External sector

5

The analyses presented in the latest issues of this Inflation Report show that the evolution of the balance of payments' flow, reflected on five consecutive years of surplus in the current account, propitiated relative changes in the country's foreign accounts, registering strong growth in the stock of international reserves and decrease in external liabilities, especially in the public sector. This new Brazilian external position, which contributes to the decrease of our economy's vulnerability to external shocks, and the continuity of consistent macroeconomic policy, favored the recognition of the country as a positive and stable environment for investors by both market and risk assessment agencies.

Confirming expectations of obtaining the investment classification by risk assessment agencies, the Standard & Poor's (S&P) raised the country's rating to investment grade in April, while the Fitch Rating ended up with the same movement in May. The investment grade granted to Brazil by two out of the three most important risk assessment international agencies mirrored the monetary policy management by the Central Bank aimed at ensuring that behavior of domestic prices would be consistent with the established targets within the current monetary system adopted by the country. In this scenario, in which building international reserves topped US$200 billion, possible relative risks to the external debt service are significantly reduced.

The slump observed in the world economic scenario since mid 2007, the worsening expectations about the US economic performance and the international financial markets volatility had a limited impact on the Brazilian economy, corroborating the importance of the macroeconomic adjustments made in recent years, especially the strengthening of the country's external position – translated in the performance of sustainability indicators, while confronting the turbulences in the international market. In this sense, the measurement of the Brazil-risk, after ending 2007 at 221 points, expanded to 305 points, on March 17, and impacted by the aggravating uncertainties of the financial markets, showing, since that date, a declining trend, reaching 187 points on June 17.

The balance of payments experienced a global surplus result of US$16.6 billion in the first five months of the year. Net inflows in the capital and financial accounts totaled US$33 billion, of which US$14 billion corresponded to foreign direct investments (FDI), which easily compensated for the debt – after consecutive surpluses since 2003 – of US$14.7 billion registered in current transactions.

It is expected that the financial conditions of the balance of payments remain strong, despite registering the first deficit in current transactions, on an annual basis, since 2002. This result is consistent with the upturn in activity presented by the domestic demand. The changes in forecasts for the external sector accounts for the year, compared to those in the previous Inflation Report, detailed in a specificappendix, stem from results of incorporation occurred until May, including net purchases carried out by the Central bank on the market, the new indebtedness position related to March, new foreign investments prospects after the investment grade classification.

5.1 Exchange operations

The foreign exchange operations carried out by the market generated a surplus of US$15.8 billion in the first five months of 2008, against US$35.1 billion in the corresponding period of the previous year. The positive balance maintained the conditions for the National Treasury strategy of obtaining resources on the market to serve its external debt and of continuing the program of repurchases of securities issued by the Republic, still allowing the Central Bank to continue with foreign currency acquisitions on the market.

In the first five months of 2008, in an environment of greater wariness to risk by investors in the international financial market of Brazilian imports, net inflows in the foreign exchange market decreased 54.9% in relation to the same period of the previous year. Net inflows in the trade segment dropped by 31.8% during the period, totaling US$24.9 billion, against US$36.5 billion in the first five months of 2007, registering growth of 5.3% in exchange transactions for exports and 40.8% in those referring to imports. In the financial segment, net outflows of US$9 billion, as compared to US$1.4 billion in the same period in 2007, increases of 44.8% in purchases and of 50.8% in foreign currency sales were registered.

Table 5.1 – Foreign exchange flows

	2006			2007	
	May	Jan-May	Year	May	Jan-May
Trade operations	6.0	36.5	76.7	2.9	24.9
Exports	14.0	74.6	184.8	14.7	78.5
Imports	8.0	38.1	108.0	11.8	53.7
Financial operations[1/]	0.9	-1.4	10.7	-2.8	-9.0
Purchases	27.9	115.1	348.3	33.9	166.6
Sales	26.9	116.5	337.6	36.7	175.6
Net flows	6.9	35.1	87.5	0.1	15.8

1/ Excluding interbank operations and Central Bank foreign operations.

The cumulative exchange surplus in the first five months of 2008 made it possible for the Central Bank's net purchases to close at US$13.2 billion, against US$47.5 billion in the corresponding period of 2007. The difference between the balance of the foreign exchange market and the Central Banks' net purchases was determined by the expansion in the bank's short position, which reached US$12.2 billion at the end of May 2008, against US$7.3 billion at the end of 2007.

5.2 Trade in goods

In May, the balance of trade turned in a US$4.1 billion surplus, registering monthly records both in exports, US$19.3 billion, and imports, US$15.2 billion, which accumulated, in the order, US$72.1 billion and US$63.4 billion in the first five months of the year, showing respective increases of 19.9% and 46.3% in relation to the corresponding period of 2007. The cumulative balance of trade in the year, indicating a growing trend on imports, dropped 48.3% using the same basis of comparison.

Table 5.2 – Trade balance – FOB

US$ million

Period		Exports	Imports	Balance	Total trade
Jan-May	2008	72 054	63 398	8 656	135 452
Jan-May	2007	60 096	43 338	16 758	103 434
% change		19.9	46.3	-48.3	31.0

Source: MDIC/Secex

The average daily balance for exports, when viewed by aggregated factor, showed expansions in all three categories, in the year. The value of daily sales of basic products grew 35.4% in relation to that observed in the first five months of 2007, followed by the ones related to semimanufactured, 22.3%, and to manufactured goods, 13.2%.

Table 5.3 – Exports by aggregate factor – FOB

Daily average – January-May

US$ million

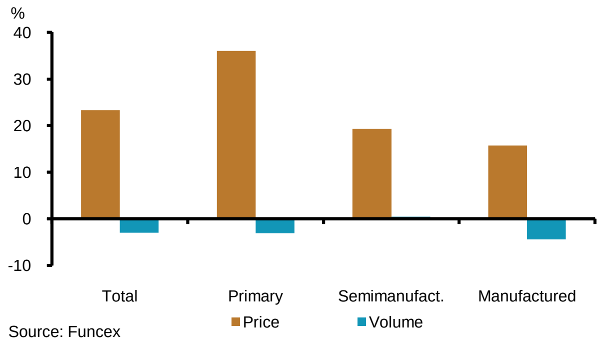
	2007	2008	% change
Total	577.8	706.4	22.2
Primary products	176.8	239.4	35.4
Industrial products	389.4	448.0	15.0
Semimanufactured goods	80.2	98.1	22.3
Manufactured goods	309.2	349.9	13.2
Special operations	11.6	19.0	63.5

Source: MDIC/Secex

Among basic products, one should mention the performance of soybean exports, 68.4%; soybean meal, 53.4%; chicken meat, 47.5%; petroleum, 25%, iron ore, 15.6%, evolution linked, to some extent, to the normalization of exports activity with the end of the customs officers strike, on May 12.

Figure 5.1 – Exports – Price and volume index

January-May – 2008/2007



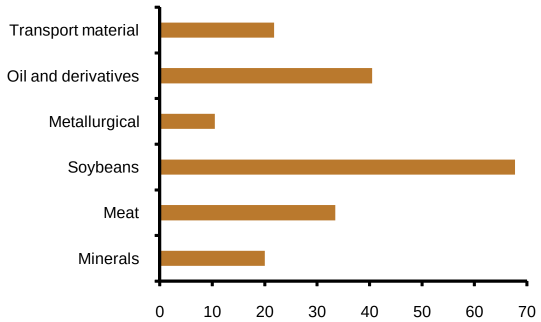
Source: Funcex

The expansion of semimanufactured good exports reflected the increase in external sales of iron alloys, 91.5%; cellulose, 49.2%; semimanufactured iron and steel products, 44%; and cast iron, 37.9%, while, in the opposite sense, raw sugar exports fell by 13.3%.

The performance of the exports of manufactured goods reflected in expansion in the sales of fuel oils, 84.4%; aircrafts, 52.3%; vehicle parts, 17.2%; and vehicles 10.2%, and, among the main items of the category, cutbacks on refined sugar exports, 20.1%; flat-rolled steel 10.5%; and footwear, 1.3%.

The performance of Brazilian exports in the year has reflected, mainly, the expansion of international prices, particularly

Figure 5.2 – Main exports
January-May – 2008/2007 – % growth



Source: MDIC/Secex

Table 5.4 – Imports by end-use category – FOB
Daily average – January-May

US$ million

Itemization	2007	2008	% change
Total	416.7	621.5	49.2
Capital goods	87.7	129.4	47.5
Raw materials	209.8	303.6	44.7
Naphtha	7.5	11.0	45.5
Consumer goods	55.3	78.3	41.4
Durable	26.3	43.3	64.8
Passenger vehicles	8.1	17.6	117.2
Nondurable	29.1	34.9	20.2
Fuels	63.8	110.3	72.7
Crude oil	39.6	59.2	49.7

Source: MDIC/Secex

commodities. According to the Foreign Trade Studies Center Foundation (Funcex), the price indices of products sold by the country grew 23.3% from January to May, compared to the same period in the previous year. On the same basis of comparison, the quantity exported registered a cutback of 3%, showing that these developments were impacted by the mentioned strike, but production should pick up, at least partially, in the next few months.

The stronger upturn in prices, observed in the basic products segment, led to growth of 36% in the analyzed period, while increases related to manufactured and semi-manufactured goods increased 15.8% and 19.3%, respectively. The most significant reduction in the exported quantity occurred in the category of manufactured goods, 4.4%, while semimanufactured products had an increase of 0.5%.

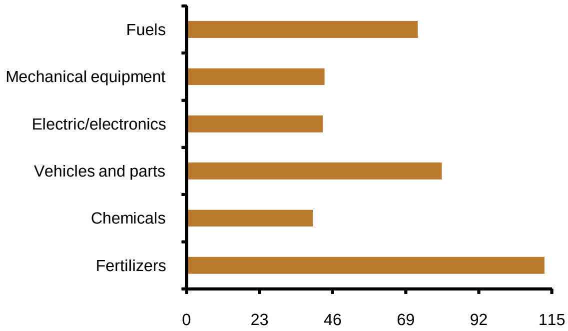
When viewed by product category, cumulative exports in the first five months of the year showed across the board increases, in relation to the same period of 2007, except for those related to sugar, which fell 14.7%, in the period. Sales related to the six most representative segments in export performance, when taken together, accounted for 58.6% of the total exported by the country in the period, showing the following growth rates: soybean, 67.7%; petroleum and derivatives, 40.5%, meat 33.5%; transportation materials, 21.8%; minerals, 20%; and metallurgical products, 10.5%.

Imports continue to show a growing trajectory in all of use categories, a movement consistent with the economic activity upturn. From January to May, external purchases grew 49.2%, considering average daily values, in relation to the same period of 2007. Consumer durables imports had the largest expansion, 64.8%, impelled by an increase of 117.2% in imports of passenger vehicles. The daily average value of raw materials and intermediate products grew 44.7%, with emphasis to transport equipment accessories, 48.1%, mineral products, 37.4%; chemical and pharmaceutical products, 37.2%, and intermediate parts and accessories, 32.3%.

The average daily imports of capital goods increased by 47.5%, in the period, a result consistent with the multiplication of investments in industry. This growth mirrored, specially, expansions registered in purchases of industrial machinery, 53.6%; office machines and apparatuses for scientific use, 34.4%; and parts and spares for industrial capital goods, 42.4%.

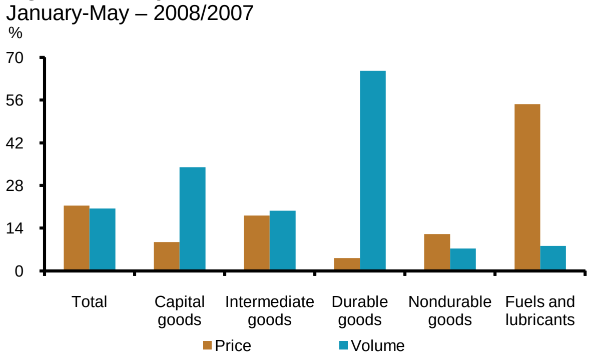
The imports of nondurable consumer goods, impacted by the upturns in pharmaceutical products, 10.8%, and

Figure 5.3 – Imports by main products
January-May – 2008/2007 – % change



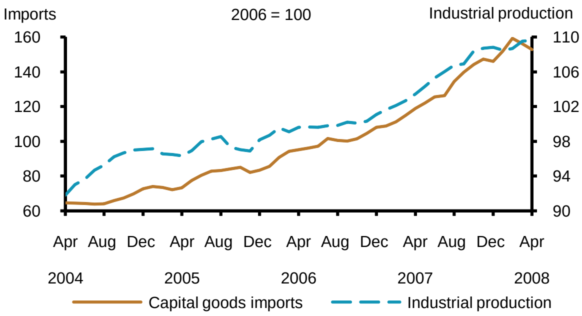
Source: MDIC/Secex

Figure 5.4 – Imports – Price and volume index
January-May – 2008/2007



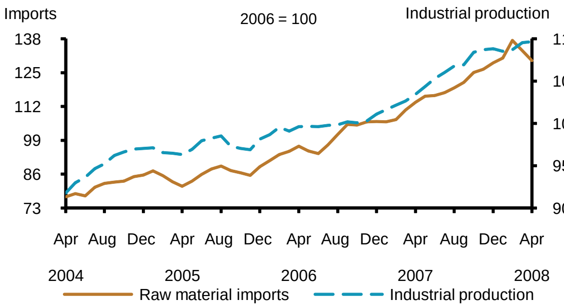
Source: Funcex

Figure 5.5 – Capital goods imports x industrial production – 3-month moving average
Seasonally adjusted indices



Sources: Funcex and IBGE

Figure 5.6 – Raw material imports x industrial production – 3-month moving average
Seasonally adjusted indices



Source:s Funcex and IBGE

foodstuffs, 28.2%; increased 20.2%, on the same basis of comparison, while purchases of fuels and lubricants grew 72.7%, impacted by the expansion of 49.7% in expenditures with external oil purchases.

The sectoral analysis of imports growth in the January-May period, compared to the corresponding period of the previous year, shows a sweeping growth of the major sectors of import list, with decrease only in the item beverage and alcohol. Considering the import daily average, it is worth noting the expansion of purchases of fertilizers, 112.6%; automotive vehicles and parts, 80.3%; fuels and lubricants, 72.7%; mechanic equipment, 43.4%; electric and electronic goods, 43%; and organic and inorganic chemical products, 39.8%. When taken together, these sectors account for 62.8% of imports in the period.

According to Funcex, the imported amount increased 20.4%, in the first five months of the year; compared to the same period in 2007, while import prices increased by 21.4%, registering different evolutions among the different categories of use. In this sense, the result of fuels and lubricants imports mirrored growth of 54.7% in prices and of 8.2% in volume. In the opposite sense, the performance of imports of consumer durables had respective increases of 4.1% and 65.6%, with emphasis to the growth in the imported amount of vehicles. Additionally, the increase in purchases of capital goods, raw materials and intermediate products and nondurable consumer goods were linked to respective growths of 34%, 19.7% and 7.3% on imported amounts and of 9.4%, 18.1% and 12.1% on prices.

The country's balance of trade with the main blocs and regions had a relative decline in comparison to the first five months of 2007, with the exception of the Mercosul Common Market (Mercosul), with which trade expansion reached by 34.3%. Trade flows, largely indicating the upward trend in imports, had a relative growth in all economic blocs and countries.

The major markets of destination of the Brazilian exports, in the first five months of the year, were still in the Euro Area, with participation of 24.9% in the total Brazilian external sales, and in the Aladi, with 22.4%; while the main single importer was the USA, with participation of 14.2%. Sales directed to China expanded 51.9%, in the period, contributing to the 40.2% growth observed in exports to Asia. During the same period, sales to Latin American Integration Association (Aladi) increased 22.8%, reaching 39.2% to the Mercosul, while exports to the European Union (EU) and the USA expanded by 21.4% and 5.3%, respectively.

Table 5.5 – Exports and imports by area – FOB

Daily average – January-February

US$ million

Itemization	Exports			Imports			Balance	
	2007	2008	% change	2007	2008	% change	2007	2008
Total	578	706	22.2	417	622	49.2	161	85
Latin America	129	158	22.8	73	104	42.8	56	54
Mercosur	59	83	39.2	41	58	41.4	18	24
Argentina	49	68	38.4	37	52	39.6	12	16
Other	10	14	43.7	4	6	58.2	6	8
Other	69	75	8.8	32	46	44.7	37	29
USA 1/	95	100	5.3	68	91	33.9	27	9
EU	145	176	21.4	94	131	39.1	51	46
E. Europe	15	20	33.5	8	18	109.2	7	2
Asia	89	125	40.2	104	170	63.9	-14	-44
China	37	56	51.9	41	70	72.1	-4	-14
Other	52	69	31.9	63	99	58.5	-10	-30
Others	104	126	21.2	69	108	55.1	35	19

Source: MDIC/Secex

1/ Includes Puerto Rico.

Table 5.6 – Current account

US$ billion

	2007			2008		
	May	Jan-May	Year	May	Jan-May	Year 1/
Current account	-0.4	0.6	-2.1	-0.6	-14.7	-21.0
Trade balance	3.6	15.4	36.4	4.1	8.7	25.0
Exports	13.4	58.8	157.1	19.3	72.1	182.0
Imports	9.8	43.3	120.6	15.2	63.4	157.0
Services	-1.2	-4.7	-13.4	-1.7	-6.8	-16.3
Transportation	-0.4	-1.8	-4.5	-0.5	-2.5	-6.5
International travel	-0.3	-0.7	-3.3	-0.6	-2.0	-5.0
Computer and informat.	-0.2	-0.9	-2.1	-0.2	-1.2	-2.3
Operational leasing	-0.5	-2.3	-5.8	-0.6	-2.5	-6.0
Other	0.1	1.0	2.3	0.1	1.3	3.5
Income	-3.2	-11.8	-29.2	-3.3	-18.1	-33.5
Interest	-0.3	-3.9	-7.3	-0.1	-2.7	-4.9
Profits and dividends	-2.9	-8.1	-22.4	-3.2	-15.6	-29.0
Compensation of employment	0.0	0.2	0.4	0.0	0.2	0.4
Current transfers	0.4	1.7	4.0	0.3	1.5	3.8

1/ Forecast.

Analysis of imports by countries and regions shows that 27.3% of the country's external purchases came from Asia, in the analyzed period, followed by those originated in the EU, 21%; Aladi, 16.8%; and the USA, 14.7%. Purchases from Asia registered higher increases in the period, 63.9%, with emphasis on those from China, representing 11.3% of the Brazilian imports, which grew by 72.1%. Imports originated in the Aladi grew 42.8% among which those from Mercosul expanded 41.4%, followed by those from the EU, 39.1%, and from the USA, 33.9%. One should still note that 109% increase in imports originated in Eastern Europe, a result that, even considering the relatively small participation of this bloc in the Brazilian total purchases, represents the continuity of a healthy diversification of our supply markets.

5.3 Services and income

The current account deficit reached US$14.7 billion in the first five months of this year, accumulating a negative result of US$15.2 billion in twelve months, 1.11% of GDP, against a US$13.4 billion surplus in the corresponding period of 2007, 1.15% of GDP. The account's growth mirrored both the balance of trade decline and the rising deficit in the services and income account, in the period.

The net remittances from services summed up US$6.8 billion, while those from income totaled US$18.1 billion, in the first five months of the year, increasing, in the order, 45.1% and 53.2% in relation to the corresponding period of 2007. Parallel to the deficit growth, one should note the rising trend of traded values both in revenues and expenditures.

Revenues referring to international travel reached US$2.5 billion and expenditures, US$4.5 billion, with respective expansions of 18.1% and 60.2% in relation to the same period of 2007. Net expenditures summed up US$2 billion in the period, against US$707 million in the first five months of the last year, a growth consistent with recent trends of available income from foreign exchange rate nominal growth. Considering the twelve-month period ended in May, the account showed net outflows of US$4.6 billion, 142.7% higher than the ones registered in the corresponding period of 2007, with expansions of 18.2% in revenues and 54.9% in expenditures, totaling, in the twelve-month period, US$5.3 billion and of US$9.9 billion, respectively, a record level.

With reference to the income account, one should note that the increase of 93.5% in net remittances of profits and dividends, which summed up US$15.6 billion in the first five months of the year, with emphasis to growth of 76.4% in gross expenditures. Net revenues of profits and dividends totaled US$30 billion in the twelve months ended in May, with gross outflows referring to direct foreign investments increasing US$9.3 billion, impelled by expansion in the financial services and automotive sectors, US$2.3 billion each, segments which were directly impacted by the turmoil in the international financial markets or have gone through periods of low profitability in foreign countries.

Net expenditures with interests, in line with the decrease in external liabilities, had a cutback of 32.1% in the five-month period ended in May, totaling US$2.7 billion. Gross revenues with interest grew 52.2% compared to the first five months of 2007, an evolution consistent with the expansion of Brazilian liabilities abroad, especially referring to the growth in international reserves, earnings on which grew 53.8% in the period, coming to US$3.1 billion.

The net unrequited transfers summed up US$1.5 billion in the first five months of the year, 7.2% lower than the level registered in the same period of 2007. In the last twelve months ended in May, these net inflows dropped 8.6%.

5.4 Financial account

In May, the balance of payments financial account posted a US$3.6 billion surplus, totaling a balance of US$32.7 billion in the year. Brazilian direct investments abroad showed net outflows of US$7.6 billion in the first five months of 2008, of which US$5.5 billion refer to equity capital and US$2.1 billion to intercompany loans.

FDI net inflows closed at US$14 billion in the first five months of the year, against US$10.5 billion in the corresponding period of the previous year, registering net inflows in the capital participation of US$8.3 billion and intercompany loans of US$5.7 billion. The FDI net inflows accumulated in twelve months summed up US$38 billion in May, the highest value in the series, a result consistent with the observed growth of investments in the industrial sector.

Foreign portfolio investments registered a surplus of US$2.3 billion in May, totaling net inflows of US$12.9 billion in the first five months of the year From this total, US$5.4 billion refer to Brazilian companies bonds negotiated

Table 5.7 – Financial account

US$ billion

Itemization	2007			2008		
	May	Jan-May	Year	May	Jan-May	Year[1/]
Capital account	15.7	49.8	88.4	3.6	32.7	41.4
Direct investments	1.3	14.0	27.5	-0.1	6.4	17.0
Abroad	0.8	3.5	-7.1	-1.4	-7.6	-18.0
In Brazil	0.5	10.5	34.6	1.3	14.0	35.0
Equity capital	0.2	8.4	26.1	0.3	8.3	26.4
Intercompany loans	0.3	2.1	8.5	1.0	5.7	8.6
Portfolio investments	4.5	19.3	48.4	2.5	12.9	19.6
Assets	-0.3	-0.1	0.3	0.3	0.0	-1.1
Liabilities	4.8	19.4	48.1	2.3	12.9	20.7
Derivatives	0.0	-0.2	-0.7	0.0	-0.3	0.0
Other investments	10.0	16.7	13.2	1.2	13.6	4.9
Assets	-2.8	-13.3	-18.7	1.0	-4.0	-20.6
Liabilities	12.8	29.9	31.9	0.2	17.6	25.4

1/ Forecast.

in the country which, after registering net outflows in January, once again showed net inflows as of March. Net revenues related to fixed-income bonds a segment negotiated in the country totaled US$9.3 billion in the first five months of the year, one should note that since mid-March, impacted by changes in legislation regulating portfolio investments, there was a strong decrease in these flows, contrasting with the growth in those channeled to Brazilian companies´ bonds.

Foreign investments in fixed income bonds negotiated abroad showed net amortizations in the first five months of 2008. Including the National Treasury repurchases program, the medium- and long-term bonds showed net amortizations of US$2.4 billion, of which US$2.7 billion refer to the bond face value and US$194 million refer to premiums of such operations. Additionally, disbursements of US$525 million were registered with reference to the Global 17 reopening, in May.

Net disbursements related to medium and long-term private bonds reached US$516 billion in May, accumulating net disbursements of US$1.8 billion in the first five months of the year, period in which short-term bonds showed net amortizations of US$1 billion.

The other Brazilian investments showed significant decrease of assets abroad in May, US$1 billion, accumulating US$4 billion of constitution in the first five months of the year, of which US$3.3 billion in currencies and deposits.

The other foreign investments had a US$195 million surplus in May, accumulating US$17.6 billion in the year. When this result is broken down, the short-term trade credit responded for net remittances of US$1.8 billion in the month and net inflows of US$8.4 billion in the first five months of the year, noting an upturn in foreign exchange contracting operations in exports, in accordance with the maturity 00of operations. Medium and long term loans summed up net disbursements of US$1.1 billion in May and of US$6.7 billion in the year, while short-terms loans registered net inflows of US$775 million and net amortizations of US$812 million, in the same periods.

International reserves grew US$17.6 billion in the first five months of the year, totaling US$197.9 billion. The Central Bank´s purchases on the foreign exchange spot market totaled US$13.2 billion while, among foreign operations, one should highlight the disbursements of US$525 billion in Republic bonds and of US$150 billion

Table 5.8 – BP financing sources
Selected items

US$ billion

	2007			2008		
	May	Jan-May	Year	May	Jan-May	Year[1/]
Medium and long-term funds	1.3	10.6	24.3	1.5	7.3	17.2
Public bonds	0.4	2.5	2.9	0.5	0.5	0.5
Private debt securities	0.6	6.4	15.4	0.7	3.9	12.2
Direct loans	0.3	1.7	6.0	0.3	2.8	4.4
Short-term loans (net)[2/]	9.4	23.5	13.8	0.8	-0.8	-3.0
Short-term securities (net)	0.3	2.8	3.7	0.0	-1.0	0.0
Portfolio (net)	4.6	1.4	45.1	1.6	14.7	25.0
Roll-over rates (%)						
Private sector:	268%	66%	109%	228%	226%	100%
Debt securities	277%	235%	186%	434%	194%	100%
Direct loans	247%	19%	53%	108%	298%	100%

1/ Forecast.
2/ Includes direct loans and trade credits transferred by banks.

Table 5.9 – Statement of international reserves

US$ billion

	2007		2008	
	Jan-May	Year	Jan-May	Year[1/]
Reserve position in previous period	85.8	85.8	180.3	180.3
Net Banco Central purchases	47.5	78.6	13.2	13.2
Debt servicing (net)	-5.3	-7.8	-1.9	0.7
Interest	-0.4	1.5	0.9	3.5
Credit	2.0	6.3	3.1	7.8
Debit	-2.4	-4.9	-2.2	-4.3
Amortization	-4.9	-9.3	-2.7	-2.7
Disbursements	2.5	2.9	0.7	0.7
Multilateral organizations	-	-	0.2	0.2
Sovereign bonds	2.5	2.9	0.5	0.5
Others[2/]	-1.4	6.9	0.6	0.6
Treasury's purchases	7.3	14.0	5.0	7.1
Change in assets	50.6	94.5	17.6	22.3
Gross reserve position	136.4	180.3	197.9	202.6

1/ Forecast.
2/ Includes payments/receipts in the framework of the Reciprocal Credits and Payments Agreement (CCR), fluctuations in prices of securities, exchange parities and price of gold, discounts and premiums, duty fees and release of collaterals.

of inflow together with the Bird, besides amortizations of US$2.7 billion of sovereign bonds, including, in this last one, US$660 million related to operations of repurchase of external debt bonds, by the National Treasury. Interest net revenues reached US$863 million, a result of gross expenditures of US$2.2 billion with bonds and revenue interests of US$3.1 billion related to earnings on international reserves. The National Treasury's net purchases summed up US$5 billion, while other operations had revenues of US$599 million.

By the end of 2008, the international revenue stock is estimated to be a total of US$202.6 billion, with annual growth of US$22.3 billion. Including the result of the first five months, net revenues are forecasted at US$0.7 billion, related to the external debt services and disbursements of US$0.2 billion contracted with companies and of US$0.5 billion related to sovereign bonds, even considering that the National Treasury will purchase US$7.1 billion on the exchange domestic market to service its external debt.

5.5 External sustainability indicators

Considering the estimated external debt position for May, the external sustainability indicators in general maintained the positive trend observed in December 2007, an evolution consistent both with increases registered in exports, in nominal GDP in dollars and in the international reserves, and with cutback in the external debt service, easily offsetting the growth in total external debt.

In the analyzed period, the external debt service decreased in US$11.4 billion, while exports grew US$12 billion, movements reflected in the fall, from 32.3% to 23.4%, registered in the participation of the debt service in the country's external sales.

The total external debt grew US$9.8 billion, in the period, while the creditor position of the net total external debt increased from US$11.9 billion to US$21 billion. Taking into account that GDP estimated in dollars grew 3.6% in the period, a growth of 0.2 p.p., to 14.9% was observed in relation to the total external debt, while the net total debt participation in GDP moved from -0.9% to -1.5%, the lowest value for the series, initiated in 1970.

The total of external debt coefficients /exports and total net external debt/exports, remained stable in the period, at 1.2

Table 5.10 – Sustainability indicators[1/]

US$ billion

	2006	2007				2008
	Dec	Mar	Jun	Sep	Dec	May[2/]
Exports of goods	137.8	142.4	150.0	153.5	160.6	172.6
Exports of goods and services	157.3	162.8	171.4	175.9	184.5	198.9
Debt service	56.9	59.4	53.6	55.4	51.9	40.4
Total external debt	172.6	182.1	191.4	195.3	193.2	203.0
Net external debt	74.8	60.0	28.9	17.0	-11.9	-21.0
International reserves	85.8	109.5	147.1	163.0	180.3	197.9
GDP	1 072	1 125	1 185	1 247	1 314	1 361
Indicators						
Total external debt/GDP (%)	16.1	16.2	16.1	15.7	14.7	14.9
Net external debt/GDP (%)	7.0	5.3	2.4	1.4	-0.9	-1.5
Total external debt/exports	1.3	1.3	1.3	1.3	1.2	1.2
Total external debt/exports of goods and services	1.1	1.1	1.1	1.1	1.0	1.0
Net external debt/exports	0.5	0.4	0.2	0.1	-0.1	-0.1
Net external debt/exports of goods and services	0.5	0.4	0.2	0.1	-0.1	-0.1
Debt service/exports (%)	41.3	41.8	35.7	36.1	32.3	23.4
Debt service/exports of goods and services (%)	36.2	36.5	31.3	31.5	28.1	20.3
Reserves/total external debt (%)	49.7	60.2	76.9	83.4	93.3	97.5

1/ Excludes stock of principal, amortizations and interests concerning intercompany loans.
2/ Estimated data.

and -0.1, respectively, the lowest results registered since the beginning of the series, in 1970.

Still in the same period, international reserves reached a level virtually identical to the total external debt, with the relation between these two indicators increasing from 93.3% to 97.5%, the series' record, an evolution linked to the growth of US$17.6 billion in the international reserves, against US$9.8 billion in the total external debt.

5.6 Conclusion

The uncertainties still prevailing in international market will impact the forecasted scenarios for commodity prices, capital flows, growth rates for exports and world output. Nevertheless, forecasts related to the country's external accounts for 2008 incorporated the prevalence of favorable balance of payments financing conditions, an expectation justified, somewhat, by the Brazilian economy experience since the second half of 2007, when the international financial markets volatility, derived from the default in the subprime market, exerted a residual impact on the country's economy.

The 2008 fiscal year will register the first current account deficit in the last five years. This result, impacted by a decrease in the balance of trade and by the increase in net remittances of services and income, especially, of, should be financed with net inflows of the balance of payments´ financial account, with emphasis on direct foreign investments. One should note, above all, that the floating exchange rate must mitigate significant movements in the country's external accounts.

The significant piling of reserves continues reducing the country's exposure to risks connected to external shocks. In this context, it is plausible to conclude that, if consistence of macroeconomic policies persists, reflected on the accreditation of Brazil´s investment grade by two large risk rating agencies, even in a scenario of more volatile external environment, the Brazilian economy meets the requirements for maintenance of this expansionist cycle.

Balance of Payments Projections

Table 1 – Uses and sources

US$ billion

	2007			2008		
	May	Jan-May	Year	May	Jan-May	Year[1]
Uses	-2.0	-18.9	-36.6	-1.7	-23.0	-51.6
Current account	-0.2	1.9	1.5	-0.6	-14.7	-21.0
Amortizations ML-term[2]	-1.9	-20.8	-38.1	-1.0	-8.3	-30.6
Securities	-1.3	-9.0	-20.6	-0.3	-5.1	-17.1
Paid	-1.3	-8.8	-19.9	-0.3	-5.1	-17.1
Refinancing	0.0	0.0	0.0	0.0	0.0	0.0
FDI conversions	0.0	-0.2	-0.7	0.0	0.0	0.0
Suppliers' credits	-0.1	-0.6	-1.5	-0.1	-0.7	-1.9
Direct loans[3]	-0.5	-11.2	-16.1	-0.6	-2.5	-11.6
Sources	2.0	18.9	36.6	1.7	23.0	51.6
Capital account	0.1	0.4	0.8	0.1	0.3	0.9
FDI	0.5	10.5	34.6	1.3	14.0	35.0
Domestic securities[4]	3.8	13.3	39.8	1.4	12.7	25.0
ML-term disbursem.[5]	1.8	12.7	36.0	3.1	14.8	34.7
Securities	1.0	8.8	18.3	1.2	4.5	12.7
Supliers' credits	0.1	0.4	1.6	0.2	1.1	4.2
Loans[6]	0.7	3.4	16.1	1.6	9.2	17.8
Brazilian assets abroad	-2.3	-9.8	-25.4	-0.1	-11.6	-39.7
Other[7]	13.6	42.7	38.4	0.0	9.4	17.0
Reserve assets	-15.5	-50.9	-87.5	-4.0	-16.6	-21.3

1/ Forecast.
2/ Registers amortization of medium and long-term supliers' credit, loans and securities placed abroad minus refinancing and discounts. Excludes amortizations referring to loans to IMF and intercompany loans.
3/ Registers amortizations loans borrowed from foreign banks, buyers, agencies and multilateral organizations.
4/ Includes foreign investment in equity and debt securities traded in the domestic market.
5/ Excludes intercompany loans disbursements.
6/ Includes multilateral and bilateral financing and buyers' credits.
7/ Registers net values of bond swaps, short-term securities, short-term trade credit, financial derivatives, nonresident deposits, other liabilites and errors & omissions.

Projections for the external accounts published in the March Inflation Report have been updated by taking into account recent statistics and the impact of the new stock of external debt calculated for the month of March, including the new schedule for amortization and interest payments.

The forecast for the current account deficit in 2008 moved upward from US$12 billion to US$21 billion, in view of the worse than expected results observed in the first months of the year, the decrease of US$2 billion in the expected trade surplus and the increase of US$7 billion in the forecast deficit for the services and income account.

With regard to the balance of trade, the estimated annual growth of exports was maintained at 13.3%, while the rise in imports, in line with the upward trend observed in domestic demand, was revised to 30.2%. Thus, the trade surplus estimate was revised to US$25 billion, as compared to US$27 billion in the March Inflation Report.

The deficit in the services account is estimated at US$16.3 billion for 2008, for a US$1.9 growth compared to the previous estimate. This result is due to an expected increase in the deficit in the transportation account, to US$6.5 billion, as a consequence of expected enhanced dynamics in the foreign trade and a rising in sea freight on a global scale. The forecast for the deficit on international travel was also raised from US$4 billion to US$5 billion, based on the expansion of net outflows occurred so far, a movement consistent with the increase in available income and the nominal exchange rate.

The forecast for 2008 net interest payments was slightly raised, to US$4.9 billion, reflecting the new scheme for payments of interest on foreign debt and the expected trajectory for interest rates and for Brazilian assets abroad. Interest revenues are expected to mount to US$11.9 billion, of which US$7.8 billion related to earnings on international reserves, while expenditures are forecast at US$16.7 billion, based on the profile of the stock of external debt calculated in March 2008.

The most significant revisions in the current account occurred under the heading profits and dividends. By analyzing its performance in the year, one may observe that the additional flows of US$7.5 billion are due mainly to remittances of direct investment income, US$5.8 billion. Nearly two thirds of this expansion was concentrated on the financial, automotive vehicles and metallurgy sectors. The estimated value for net remittances of profits and dividends has been revised from US$24 billion to US$29 billion, the same level reached by the 12-month accumulated net outflows in the month of May, reflecting the expected of stabilization of these flows at current levels. The performance of expenditures continues to be influenced by the growth in the stock of foreign investments in the country, by the business profitability, in contrast to that observed in mature economies, and by the trajectory of the exchange rate. It is reasonable to attribute a pro-cyclical nature to this component of the current accounts, since remittances tend to intensify at periods of economic heating and to diminish in periods of economic accommodation, thus establishing an endogenous adjustment factor for the current account in relation to the domestic economic cycle.

The balance of payments financial account is expected to register a surplus of US$41.4 billion, US$17 billion higher than the March forecast, reflecting the improvements observed in the first five months of the year and the expected rise in the inflows of foreign direct and portfolio investments, the occurrence of net disbursements in other investments and expansion of the commercial banks' assets abroad. International reserves should close the year at US$202.6 billion, an increment of US$22.3 billion as compared to the end of 2007.

Table 2 – Balance of payments – Market

US$ billion

Itemization	2007			2008		
	May	Jan-May	Year	May	Jan-May	Year[1/]
Current account	-0.6	0.6	-4.8	-1.3	-17.8	-28.8
Capital (net)	17.8	54.4	94.1	2.2	33.2	58.8
Foreign direct investment	0.5	10.5	34.6	1.3	14.0	35.0
Portfolio investment	3.8	13.3	39.8	1.4	12.7	25.0
Medium and long term loans	-0.5	-10.4	-9.8	0.4	1.6	-3.7
Trade credits – Short, medium and long term	12.2	37.1	36.1	-0.1	11.8	24.1
Banks	9.5	23.6	18.6	1.6	3.0	1.8
Other	2.7	13.6	17.5	-1.7	8.8	22.3
Brazilian investment abroad	0.2	-3.1	-14.8	-1.7	-9.3	-22.9
Other	1.6	6.9	8.3	0.8	2.5	1.3
Financial gap	17.2	54.3	89.3	0.9	15.4	30.0
Banco Central net intervent.	-14.6	-47.5	-78.6	-2.5	-13.2	-13.2
Bank deposits	-2.5	-6.8	-10.7	1.6	-2.2	-16.8

1/ Forecast.

As a result of the process of internationalization of Brazilian companies, which has accelerated in 2008, the forecast for the remittances of Brazilian direct investments abroad was raised from US$10 billion to US$18 billion, while foreign direct investment inflows are estimated at US$35 billion for the entire year, a result slightly higher than the record set in 2007 and higher than the forecast of US$32 billion calculated in the March 2008 Inflation Report.

The forecasts for medium and long-term external debt repayments were revised upward from US$28.7 billion to US$30.6 billion, reflecting the March profile of the stock of external debt, the forecast performance for the exercise of put/call options and the incorporation of the impact of repurchase operations carried out by the Treasury in the first four months of the year.

Projected medium and long-term investments in domestic stocks and papers were revised upward to US$25 billion, an increase consistent with the changes occurred in the first five months of the year and the expectations of investment grade ratings to be granted by two of the three largest international risk assessment agencies. Rollover rates for the medium and long-term private debt were maintained at 100%.

The total banking sector assets abroad are expected to increase US$16.8 billion in 2008, compared to US$5.6 billion estimated in March, primarily as a result of the rise in direct and foreign portfolio investments. Therefore, the balance of payments is expected to register a surplus of US$21.3 billion in 2008, compared to the US$13.4 billion March estimate. This result is consequent upon the incorporation of net purchases of foreign currency carried out by the Central Bank on the market in the first five months of the year and supposes that the Central Bank will no longer carry out additional currency purchases on the market and that the Treasury will fully serve its foreign debt by raising funds in the market. Therefore, the performance of the external accounts is expected to permit an adequate financing of the balance of payments in 2008.

Table 2 – Balance of payments – Market

US$ billion

Itemization	2007			2008		
	May	Jan-May	Year	May	Jan-May	Year[1/]
Current account	-0.6	0.6	-4.8	-1.3	-17.8	-28.8
Capital (net)	17.8	54.4	94.1	2.2	33.2	58.8
Foreign direct investment	0.5	10.5	34.6	1.3	14.0	35.0
Portfolio investment	3.8	13.3	39.8	1.4	12.7	25.0
Medium and long term loans	-0.5	-10.4	-9.8	0.4	1.6	-3.7
Trade credits – Short, medium and long term	12.2	37.1	36.1	-0.1	11.8	24.1
Banks	9.5	23.6	18.6	1.6	3.0	1.8
Other	2.7	13.6	17.5	-1.7	8.8	22.3
Brazilian investment abroad	0.2	-3.1	-14.8	-1.7	-9.3	-22.9
Other	1.6	6.9	8.3	0.8	2.5	1.3
Financial gap	17.2	54.3	89.3	0.9	15.4	30.0
Banco Central net intervent.	-14.6	-47.5	-78.6	-2.5	-13.2	-13.2
Bank deposits	-2.5	-6.8	-10.7	1.6	-2.2	-16.8

1/ Forecast.