

International Financial Crisis – Brazilian government's performance in the provision of liquidity in foreign currency

In mid-September, with the bankruptcy of Lehman Brothers bank, the worsening of the international financial crisis impacted significantly the supply of international financing lines, as well as the costs and terms of the remaining credit lines. In this scenario, coupled with an increased wariness to risk and the need by foreign investors in the country to offset losses in their head offices, expressive net outflows in the domestic foreign exchange market were registered in October and November, affecting both the level and volatility of the exchange rate.

In this environment, as of September 18, the Central Bank, looking to highlight the temporary nature of the measures and reaffirm its commitment with the floating exchange rate, began to intervene in the exchange market, by announcing auctions of repurchase lines. On October 10, the Central Bank, in order to make it clear that the provision of liquidity in foreign currency aimed at normalizing the domestic market, informed that there were no previously limits fixed for its intervention.

Among the measures implemented to meet the liquidity needs in foreign currency are the return of sale interventions on the foreign exchange spot market; the aforementioned repurchase lines, which can be described as auctions for FX sales with repurchase commitment, and the creation of the FX loans modality, guaranteed by sovereign bonds negotiated on the international market or by export operations, the resources of which must be targeted to the financing of exports.

Table 1 summarizes the operations effectively carried out up to December 1st. Figures 1 and 2 describe the daily values of the measures contracted, by modality,

Table 1 – Supply of foreign currency liquidity

Up to 12.1.2008

	US\$ million
Forex liquidity measures	
Spot market interventions	6 698
Repurchase lines	10 690
Forex loans – Global	1 519
Forex loans – ACC/ACE	0
Total	18 907
Amount repurchased	
Repurchase lines	-500
Forex loans – Global	0
Forex loans – ACC/ACE	0
Repurchase total	-500
Net total	18 407

and accumulated values in the period. The measures announced as well as their details are enumerated in the sequence.

1) FX loans

On October 6, Provisional Measure n. 442, which authorizes the National Monetary Council (CMN) to establish special criteria and conditions for the assessment and acceptance of assets by the Central Bank as guarantee in FX loan operations. According to the Provisional Measure n. 442, these guarantees should be denominated and referenced in the same currency as in which the loan is granted and that, in a complementary nature, these guarantees could be alienated through public offer, with the Central Bank incorporating the result to its balance sheet.

Figure 1 – Measures aiming at Forex Liquity

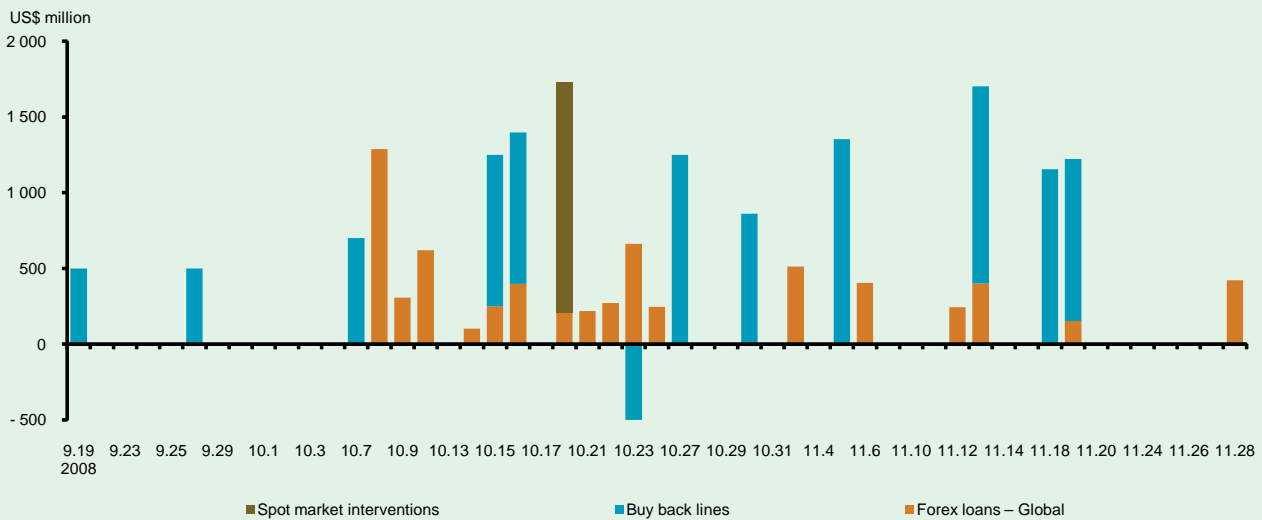
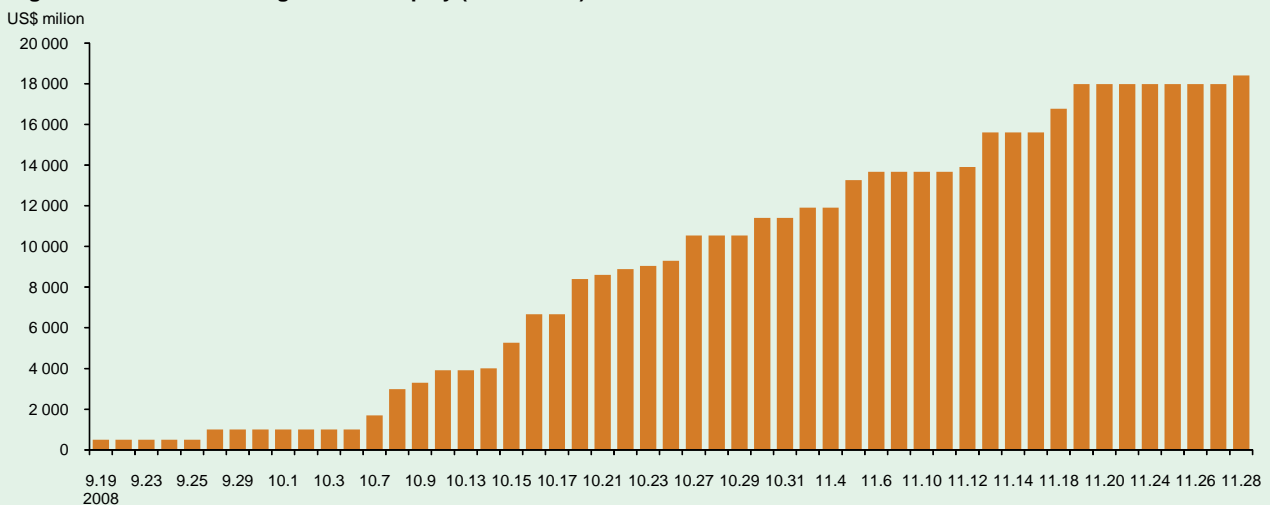


Figure 2 – Measures aiming at Forex Liquity (cumulative)



On October 9, the National Monetary Committee published Resolution n. 3,622, regulating the FX loans. These loans were limited to 360 days, including renewals, at the Libor cost added with a percentage fixed by the Central Bank according to market conditions. The guarantees were defined in two modalities, namely: i) sovereign bonds denominated in dollars issued by Brazil and countries with rating equal or above A and ii) Advances on Exchange Contracts (ACC), Advances on Exchange Deliveries (ACE), and other external financing modalities. Later, through Resolution n. 3,624, dated October, 16, the CMN determined that the Central Bank should decide whether the resources are to be directed, total or partially, to foreign trade operations.

Until December 1st, one auction of FX loan backed in Brazilian sovereign bonds (Globals) and three backed in ACC/ACE were carried out. With regard to the latter, the auction's operational guideline foresees that repurchase line operations be carried out with a term of approximately 30 days. During this period, as the banks are responsible for funding ACC/ACE operations, the effective amount received in the form of FX loan will, in this case, be equal to the foreign trade operations effectively offered by the bank. Total amounts offered reached US\$5.3 billion, of which US\$1.5 billion in the Globals auction and US\$3.8 billion in the ACC/ACE auctions. One should highlight that the latter refers to the auctions results, since these loans will be granted only on December 8, 17 and 19, respectively.

Table 2 – Foreign exchange loans – Globals

Auction date	Settlement			Cut rate	Accepted bids	Value US\$ million
	Loan	Amortization				
10.20.2008	10.27.2008	4.20.2009	175	Libor+0,11%	2	1 000
10.20.2008	10.28.2008	4.20.2009	174	Libor+0,11%	1	500
10.20.2008	11.4.2008	4.20.2009	167	Libor+0,11%	1	19
TOTAL					4	1 519

Table 3 – Foreign exchange loans – ACC/ACE

Auction date	Settlement			Cut rate	Accepted bids	Value US\$ million
	Loan	Amortization				
11.5.2008	12.8.2008	5.8.2009	151	Libor+1%	18	...
11.13.2008	12.17.2008	11.12.2009	330	Libor+1,5%	12	...
11.18.2008	12.19.2008	11.13.2009	329	Libor+1,1%	9	...
TOTAL					39	0

2) Repurchase lines

On September 18, the Central Bank Governor announced that the Institution would resume the USD sale on the spot market by means of auctions to dealers, with repurchase commitment. Operationally, once the auction result is released, of which the purchase is limited to 25% of the total per dealer, sale and purchase exchange contracts are formalized, in the same values, with settlements for D+2 (sale) and established date (purchase). One should highlight that, after the release of Circular n. 3,412, dated October 13, the bank that purchases FX will be exempt from the compulsory collection due on Interfinancial Leasing Deposits in the amount of the equivalent in BRL and for the term of the operation, if carried out as of that date, neutral in relation to liquidity in national currency. Auctions, which totaled US\$10.7 billion, are detailed on Table 4. It should be noted that there was already repurchase of the US\$500 million related to the first auction and that the auctions dated October 5, 13 and 18 were those of FX loans against ACC/ACE, the first phase of which foresees the carrying out of repurchase lines.

Table 4 – Repurchase line

Auction date	Settlement		Value US\$ million
	Sale	Purchase	
9.19.2008	9.23.2008	10.23.2008	500
9.26.2008	9.30.2008	12.19.2008	500
10.7.2008	10.9.2008	1.7.2009	700
10.15.2008	10.17.2008	1.15.2009	1 000
10.16.2008	10.20.2008	4.20.2009	1 000
10.27.2008	10.29.2008	1.2.2009	750
10.27.2008	10.29.2008	2.2.2009	500
10.30.2008	11.3.2008	2.2.2009	860
11.5.2008	11.7.2008	12.8.2008	1 353
11.13.2008	11.17.2008	12.17.2008	1 302
11.18.2008	11.20.2008	12.19.2008	1 155
11.19.2008	11.21.2008	1.2.2009	110
11.19.2008	11.21.2008	2.2.2009	130
11.19.2008	11.21.2008	3.2.2009	830
TOTAL			10 690

3) Sale interventions

In addition, the Central Bank carried out auctions for USD sales on the spot market. These operations look

Table 5 – Spot market sale intervention

Auction date	Settlement	Value US\$ million
10.8.2008	10.10.2008	1 287
10.9.2008	10.14.2008	307
10.10.2008	10.15.2008	620
10.14.2008	10.16.2008	102
10.15.2008	10.17.2008	250
10.16.2008	10.20.2008	398
10.20.2008	10.22.2008	210
10.21.2008	10.23.2008	218
10.22.2008	10.24.2008	270
10.23.2008	10.27.2008	662
10.24.2008	10.28.2008	245
11.3.2008	11.5.2008	511
11.6.2008	11.10.2008	403
11.12.2008	11.14.2008	243
11.13.2008	11.17.2008	400
11.19.2008	11.21.2008	152
11.28.2008	12.2.2008	421
TOTAL		6 698

to provide liquidity at critical moments in which the domestic financial markets face significant shortage of foreign currency, following the principles of not interfering with the trajectory of the exchange rate, not setting floors or ceilings for this rate, and not adding volatility to the market. Obviously, these operations contract the liquidity in national currency in the amount equivalent to the expanded liquidity in foreign currency. Up to that date, these operations totaled US\$6.7 billion.

4) Swap of currencies with the Federal Reserve

On October 29, the Central Bank and the Fed released an agreement for swap of currencies in the total amount equivalent up to US\$30 billion, with term up to the end of April 2009. This swap, which the Fed had already established with diverse central banks of developed countries, aimed to offer external USD lines to countries in which financial markets experience scarcity of international financing lines termed in that currency. On the same date, terms and amounts, the Fed also agreed upon equivalent procedures with the central banks of Mexico, South Korea, and Singapore. It is relevant to highlight that this measure are targeted to countries deemed systemically important and with consistent macroeconomic policies, and that the measure does not imply a conditioning factor for the domestic economic policy. The Brazilian Central Bank has not yet made use of these resources.

Table Summary of the recent government measures aimed at providing liquidity in foreign currency (FX)

Date	Normative	Summary description	Impact actual/estimated
October 6, 2008	MP 442	Enables the CMN to establish criteria for the acceptance of assets by the Central Bank as guarantee for FX loans In the operations of FX loans, the Central bank is authorized to release the value of the operation in the same FX in which the assets received as guarantee were denominated or referenced in. As a complementary measure, other guarantees may be accepted. In case of delinquency, the Central Bank may alienate the assets through public offer, and the result should be incorporated to its balance sheet. Exempts from the requirements of fiscal regularity, except for social security (CF art. 195, § 3º) for one year.	There are no fixed limits for the intervention in the FX markets (according to press release dated September 18)
October 9, 2008	Circ. 3,622	Defines the criteria for acceptance of assets by the Central Bank as guarantee for FX loans. Operations will be carried out exclusively with banks, upon request and at the sole discretion of the Central Bank. The term of the operations, including renewals, will be of 360 days. In the FX loan operations, the cost will be Libor rate plus a percentage set by Central Bank. The guarantees for these loans are: - Global Bonds or sovereign bonds in dollars from countries rated at least A, in the amount of 105% of the loan value; - ACC, ACE, import financing and transfers (Res. 2,770), in the percentages of 120%, 130% and 140% for clients rated, respectively, AA, A and B. FX loans imply assuming an irrefragable commitment of sale of the assets given as guarantee in case of delinquency.	
October 13, 2008	Circ. 3,412	Banks will be allowed to deduct compulsory collections over DI Leasing in the value of the FX acquisitions with resale commitment, for the operations terms.	Total balance of this modality reached R\$20.1 billion on Oct.10
October 16, 2008	Circ. 3,624	The Central Bank may determine that the resources granted in FX may be directed, partial or totally, to foreign trade operations.	
October 16, 2008	Circ. 3,415	Deals with FX loan operations (MP 442, Res. 3,622 and Res. 3,624) FX loan operations will be carried out through auctions by banks authorized to operate in foreign exchange, which will define, inclusively, the spread over Libor rate. In case of maturity expiration of assets given as guarantee during the period of the operation, the bank may complement the guarantee or pay off the corresponding value. The bank may be held responsible for the management of assets given as guarantee.	
October 21, 2008	MP 443	Authorizes the Central Bank to carry out swap operations with other central banks within the limits set by the CMN.	
October 22, 2008	Decree 6,613	Reduced from 0.38% to zero the IOF rate levied upon the foreign exchange operations related to foreign loans and from 1.5% to zero upon investments of resources on the financial and capital markets.	
October 30, 2008	Res. 3,631	Limited to US\$30 billion the maximum value of operations derived from swap currency contracts formalized between the Central Bank and the Federal Reserve Bank of New York (Fed). Defined that such operations may be carried out up to April 30, 2009. BRL received by the Fed shall be credited in a Central Bank account and the dollars received by the Central Bank shall be credited on an account maintained at the Fed. Exchange rate for purchasing USD and selling BRL shall be the same as that for future resale and repurchase. These operations are not constrained by any conditioning factors of political-economic nature or other interests.	Up to US\$30 billion
November 3, 2008	Res. 3,633	It modified Resolution 3,622, dated October 3, 2008. In FX loan operations, the amounts of guarantees were altered in the following manner: - reduced from 105% to 100% for Global bonds or sovereign bonds in dollars from countries with long-term rating equivalent at least to grade A; - for ACC, ACE, import financing and transfers (Res. 2,770), the percentages were reduced from 120%, 130% and 140% for clients rated, respectively, AA, A e B, to 100%. In addition, the Resolution allowed the Central Bank to require supplementation of previous guarantees with federal public securities or other assets denominated in national currency up to the limit of 140% of the loan value. It refers to loan operations in foreign currency (Res. 3,622) with guarantees represented by ACC and ACE operations.	
November 4, 2008	Circ. 3,418	The formalization of this loan will be conditioned to the granting of ACC and ACE by utilizing the resources obtained in the operation of repurchase lines.	
November 26, 2008	Res. 3,641	Revoked Res. 3,547, dated March 12, 2008, which obligated the contracting of FX simultaneous operations in the internal migrations of investments by non-residents originally carried in variable income toward investment in fixed income or in derivatives with fixed earnings.	

(Continues)

Table Summary of the recent government measures aimed at providing liquidity in foreign currency (FX)

(concluded)

	Repurchase lines	On September 18, the Central Bank Governor announced that the Central Bank would resume the sale of dollars on the spot market through auctions to dealers with repurchase commitment. Auctions of FX loans guaranteed by ACC/ACE, of which the operational guidelines foresee, initially, the carrying out of repurchase lines reached US\$3.8 billion.	US\$10.7 billion, of which US\$3.8 billion related to FX loans with guarantees in ACC/ACE (actual)
	Sale Interventions	As of October 8, the Central Bank carried out 17 auctions for USD sale on the spot market.	US\$6.7 billion (actual)
	FX loans in guaranteed by Globals	One auction of such modality was carried on October 10. Four proposals were accepted and the cut-off rate was defined at 0.11% above the Libor. Amortization will occur on April 20, 2009.	US\$1.5 billion. (actual)
	Foreign Exchange Swap	As of October 6, resumption of FX swaps offered to the market.	US\$37.1 billion, including US\$1.5 billion in non-rolled over FX swaps (actual)