5 External sector

Current transactions, after five consecutive surpluses, once again registered a deficit in 2008. The reversal of the positive results, initiated in mid-2007, evidenced the impact of the Brazilian economy's recent trajectory of expansion over the growth rates of imports, which have been maintained at a level significantly higher than exports, and the expansion in net remittances of services and incomes, especially those related to profits and dividends.

The performance of the balance of payments' financial account continues translating a considerable FDI net inflows, which should reach a record volume in 2008, in contrast with recent outflows of external capitals related to portfolio investments, especially securities; short-term loans; and low rollover rate of the medium- and long-term external debt. In this context, the permanence of the current external scenario should turn the balance of payments financing conditions more adverse in the medium-term.

In this environment of increasing risk aversion, the forecasts related to the country's balance of payments for 2009 – see box Forecasts for the Balance of Payment on page 114 of this Report – started to incorporate the prospects for a reduction in the world economic activity, a scenario for exchange rate depreciation, the return of foreign portfolio investments, growth in country-risk indicators, shortening of financing terms, and, also, the tightening of credit supply. Additionally, for 2008 the results that took place up to November were incorporated, including the interventions by the Central Bank in the domestic foreign exchange market, as well as in the new September external indebtedness position.

One should highlight that, as of September, in response to the new conditions of the international financial market, the Central Bank has acted in order to maintain on adequate levels the liquidity in foreign currency in the country and the supply of credit line to exporters. The details of such measures can be found in the box International Financial

Crisis – Brazilian Government's Response in the Supply of Foreign Currency Liquidity, page 98 of this report.

5.1 Exchange

Table 5.1 – Foreign exchange flows

US& billion

Itemization	2007			2008	
	Nov	Jan-Nov	Year	Nov	Jan-Nov
Trade operations	7.3	73.5	76.7	3.1	48.0
Exports	17.2	170.7	184.8	13.5	176.6
Imports	9.9	97.3	108.0	10.4	128.6
Financial operations[1/]	-2.0	8.6	10.7	-10.3	-42.6
Purchases	32.3	306.7	348.3	18.7	385.9
Sales	34.3	298.1	337.6	29.0	428.5
Net flows	5.3	82.1	87.5	-7.2	5.4

1/ Excluding interbank operations and Central Bank foreign operations.

Foreign exchange operations turned in a surplus of US$5.4 billion in the first eleven months of the year, against US$82.1 billion in the corresponding period of 2007, a downturn resulting from the effects of the international financial turmoil on international investors' risk aversion and to the increased contracting of import operations. Net inflows in the trade segment fell 34.6%, to US$48 billion, in the period, while net flows in the financial segment showed inflow reversal, from UR$8.6 billion, in the first eleven months of 2007, to outflows of US$42.6 billion. The result of the trade segment is consistent with expansions of 3.4% in the contracting export operations and 32.2% in those related to imports. At the same time, the financial segment showed expansions of 25.8% in purchases and 43.7% in sales of foreign currency.

The exchange surplus accumulated in the first eleven months of 2008 made possible Central Bank net purchases of US$12.4 billion on the spot market, against US$76.3 billion in the corresponding period of 2007. The bank's long position reached US$2.5 billion, up to the end of November 2008, against US$7.3 billion at the end of 2007.

5.2 Trade in goods

Table 5.2 – Trade balance – FOB

US$ million

Period		Exports	Imports	Balance	Total trade
Jan-Nov	2008	184 125	161 667	22 458	345 792
Jan-Nov	2007	146 418	110 023	36 396	256 441
% change		25.8	46.9	-38.3	34.8

Source: MDIC/Secex

In November, exports summed up US$14.8 billion and imports, US$13.1 billion, in November, record values for that month, turning in a US$1.6 billion surplus and a trade flow of US$27.9 billion. External sales reached US$184 billion in the first eleven months of the year, increasing 25.8% in relation to the corresponding period of 2007, while external purchases expanded 46.9%, to US$162 billion, causing a cutback of 38.3% in the trade surplus, which totaled US$22.5 billion.

The exports' daily average increased 25.2% in the first eleven months of 2008, in relation to the corresponding period of 2007. The shipments of basic products, whose participation in the total exported grew from 31.9% to 37.1% in the period, increased 45.5% with emphasis on the growth of petroleum sales, 63.2%; soybeans, 62.3%; iron ore and iron ore concentrates, 60.8%; soybean, 53.1%, chicken meat, 43.2%; accounting for altogether for 70.5% of the category's exports

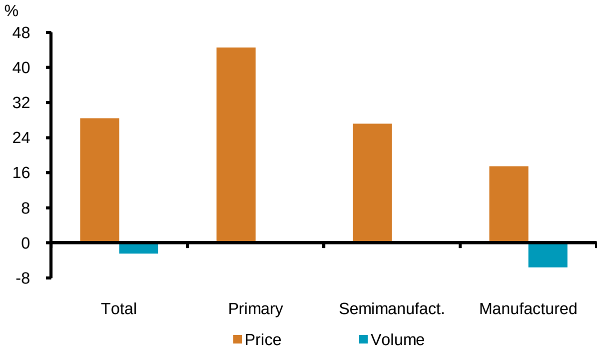
Table 5.3 – Exports by aggregate factor – FOB
Daily average – January-November

US$ million

Itemization	2007	2008	% change
Total	636.6	797.1	25.2
Primary products	203.1	295.6	45.5
Industrial products	420.6	480.3	14.2
Semimanufactured goods	87.0	110.5	27.0
Manufactured goods	333.6	369.8	10.9
Special operations	12.9	21.2	64.0

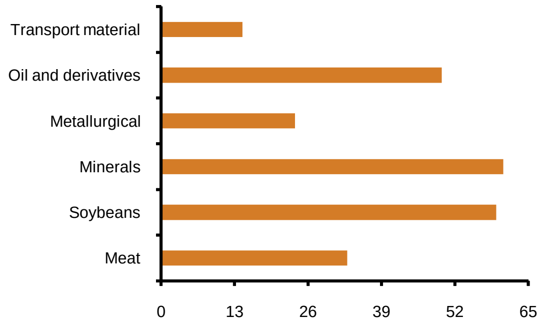
Source: MDIC/Secex

Figure 5.1 – Exports – Price and volume index
January-November – 2008/2007



Source: Funcex

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



Source: MDIC/Secex

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

US$ million

Itemization	2007	2008	% change
Total	478.4	699.9	46.3
Capital goods	99.5	143.7	44.4
Raw materials	236.6	338.3	43.0
Naphtha	7.7	9.6	24.9
Consumer goods	63.5	90.2	42.1
Durable	32.6	51.3	57.3
Passenger vehicles	12.0	21.6	79.5
Nondurable	30.9	38.9	26.1
Fuels	78.8	127.7	62.0
Crude oil	46.9	67.5	43.9

Source: MDIC/Secex

during the period. One should note that the performance of sales of basic products was linked, especially, to the price rise. One should note that the coming into force, since April, of the iron ore price increases already negotiated since the beginning of the year. Additionally, the petroleum exported quantity fell 4.5% in the period.

The exports daily average of semi-manufactured products increased by 27% in the first eleven months of the year, representing 13.9% of the total exported, against 13.7% in the corresponding period of 2007. One should note that the expansions registered in the exports of cast iron and Spiegel iron, 79.2%; semi-manufactured products of iron or steel, 77.7%; iron alloys, 70%; cellulose, 34.9%; and raw sugar cane, gross, 10.5%, representing altogether 62.9% of the category's sales.

The average exports of manufactured items, which showed generalized growth in prices, represented 46.4% of the external sales in the first eleven months of the year, increasing 10.9% in relation to the corresponding period of 2007. One should highlight growth in the sales of ethyl alcohol, 60.6%; tractors, 26.5%;engines, generators, and electric transformers, 26.1%; fuel oils, 23.7%; and aircraft, 14.3%, responsible, altogether, for 15.9% of the category's sales. One should emphasize, in the period, reduction in the shipped volume of the majority of this group's relevant products, except for the expansions linked to the items, ethyl alcohol, 44.4%, and aircraft, 7.6%.

Statistics of the Foreign Trade Studies Center Foundation (Funcex) show that the export prices grew 28.4% from January to November 2008, in relation to the corresponding period of 2007, while the exported amount dropped 2.5%. The prices of basic products increased 44.5%, followed by those related to semi-manufactured, 27.2%, and manufactured, 17.5%. The performance of the exported *quantum* translated retractions of 5.6% in the category of manufactured items, while the exported *quantum* of basic and semi-manufactured products, showed stability, in the period.

The analysis of the average external sales in the first eleven months of the year, considering the industrial sectors, shows a generalized expansion in comparison to the corresponding period of 2007, except for the reduction observed in the segments, wood, 16.1%, and leather and footwear, 5.7%. The six most representative sectors of the country's export agenda accounted for, taken together, 61.3% of the exports, with emphasis to the growth of 60.5% linked to the sales of ores, followed by the ones related to soybean, 59.3%; petroleum and derivatives, 49.6%; meat, 32.9%; metallurgical products, 23.7%; and transportation material, 14.4%.

The exports daily average grew 46.3% in the first eleven months of the year, as compared to the corresponding period of 2007, impelled, somewhat, by expansions, in the purchases of fuels and lubricants, 62%, reflecting the high level of petroleum prices in the first three quarters of the year; and 57.3% in the ones related to durable consumer goods, in line with the 79.5% growth in vehicle acquisitions.

Daily average imports of capital goods grew 44.4% in the period, with emphasis on the expansion of 76.3% experienced by the segment mobile equipments for transportation, evincing purchases of high unit value, of engines and aircraft. At the same time, one should highlight increased purchases of industrial machines, 51.5%; parts and spares of capital inputs for the industrial sector 31.8%; as well as office machines and scientific services equipment, 31.7%.

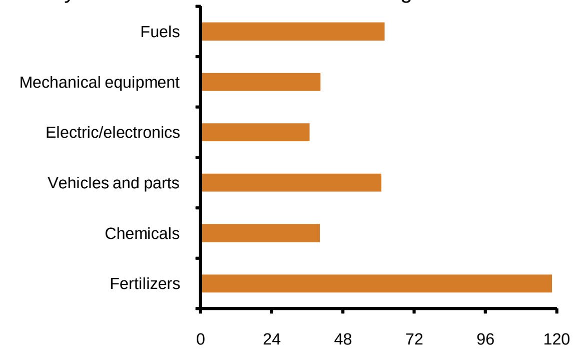
Purchases of raw materials and intermediate products, representing 48.3% of the total imported, increased 43% in the year, impelled by the purchase of raw materials for farming, 109%, a segment which includes fertilizers; and of construction materials, 62.1%. Exports of nondurable consumer goods expanded 26.1%, in the period, with highlights to the increases in the item foodstuffs, 37.3%, and textiles, 29.7%.

According to the Funcex, the amount and prices of imports registered respective growth of 22.8% and 19.5% in the first eleven months of the year, as compared to the same period of the previous year. Import growth in durable and capital goods mirrored, especially, the expansion of 50.6% and 37.1%, observed in the respective categories' volume, against increases, in the same order, of 6.9% and 8.9% in prices.

The purchases of nondurable consumer goods reflected increases of 11.1% in the imported volume and 14% in prices, while acquisitions of raw materials and intermediate products mirrored respective expansion rates of 18.8% and 20.9%. Additionally, the trajectory of purchases of fuels and lubricants derived from the 51.3% expansion in prices and 2.6% growth in the imported volume.

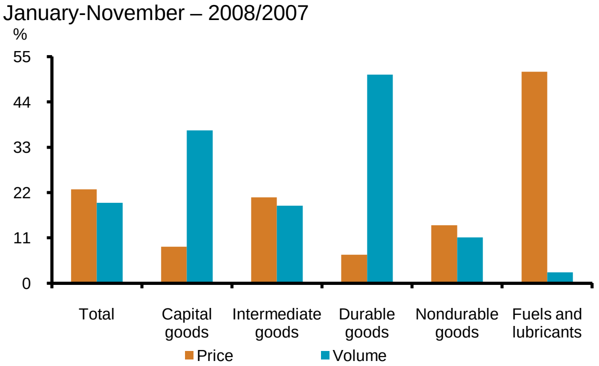
The sector analysis shows the across-the-board growth of the external purchases' daily averages in the first eleven months of the year, compared to the same period of the previous year. One should highlight the performance of the segments fertilizers, 118%; fuels and lubricants, 62%; automotive

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



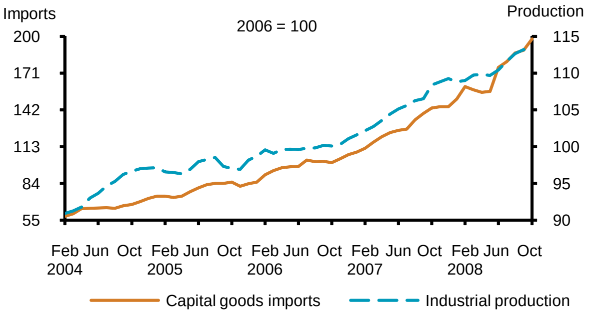
Source: MDIC/Secex

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



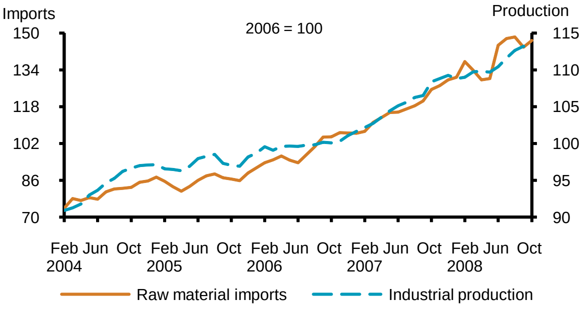
Source: Funcex

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



Source: Funcex and IBGE

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



Source: Funcex and IBGE

Table 5.5 – Exports and imports by area – FOB
Daily average – January-November

US$ million

Itemization	Exports			Imports			Balance	
	2007	2008	% change	2007	2008	% change	2007	2008
Total	637	797	25	478	700	46	158	97
Laia	144	173	20	81	110	36	63	63
Mercosur	69	89	29	45	60	33	23	28
Argentina	57	72	26	41	54	32	17	19
Other	12	16	41	5	7	40	7	10
Other	75	84	12	35	50	41	40	35
USA[1/]	100	112	12	76	103	36	25	9
EU	160	187	17	107	146	37	53	41
E. Europe	17	23	36	11	22	102	6	1
Asia	101	152	51	122	191	57	-22	-39
China	44	68	55	50	81	62	-6	-13
Other	57	84	48	72	111	53	-15	-26
Others	115	150	30	82	128	55	33	22

Source: MDIC/Secex

1/ Includes Puerto Rico.

vehicles and parts, 60.9%; mechanic equipment, 40.4%; organic and inorganic chemicals, 40.2%; and electric and electronic appliances, 36.7%.

The country's external trade flow with the main blocs and regions increased in the first eleven months of 2008, against the same period of the 2007, while the cutback of 38.6% registered in trade surplus, for a daily average of US$97 million, mirroring the occurrence of an overall reduction in the trade balances, with the exception of 21% growth in the surplus with the Southern Common Market (Mercosul).

The European Union and the Latin American Integration Association (Aladi) were the main destinations of Brazilian products, observing, in the order, 23.5% and 21.7% of the country's exports. At the same time, the United States participation, our main individual importer, followed a downward trajectory and remained at 14.1%, dropping 1.7 p.p. as compared to what happened in the first eleven months of 2007. The daily average sales to China grew 55% in the period, increasing its market-share in 1.6 p.p., to 8.5% only 0.5 p.p. lower than Argentina's, the second largest buyer. Using the same basis of comparison, the average daily exports to Asia and Aladi grew 51.3% and 20.1%, respectively, with emphasis on the 28.6% expansion in sales targeted to the Mercosul.

A breakdown of the Brazilian imports by country and region evinces an ongoing process of concentration of purchases originating in Asia, the main supplier region to the country, whose participation increased 1.8 p.p. in the first eleven months of the year, accounting for 27.4% of the total imports total, with emphasis to the increase of 61.8% in purchases from China, responsible for 11.6% of the purchases carried out by the country. One should still highlight, the expansion of 36% in the imports from Aladi member countries, a result of increases of 32.5% in the imports coming from the Mercosul member countries and of 40.1% in those coming from countries that are not part of this bloc. Imports coming from West Europe grew 102% in the year, representing 3.1% of the total.

5.3 Services and income

The deficit in current transactions accumulated in twelve months reached US$26.3 billion in November, 1.67% of GDP, against surplus of US$2.6 billion, 0.20% of GDP, in the corresponding period of 2007, a reversal linked to the

Table 5.6 – Current account

US$ billion

Itemization	2007			2008			2009
	Nov	Jan-Nov	Year	Nov	Jan-Nov	Year[1/]	Year[1/]
Current account	-1.3	2.2	1.7	-1.0	-25.8	-29.6	-25.0
Trade balance	2.0	36.4	40.0	1.6	22.5	23.5	14.0
Exports	14.1	146.4	160.6	14.8	184.1	200.0	193.0
Imports	12.0	110.0	120.6	13.1	161.7	176.5	179.0
Services	-1.2	-11.9	-13.1	-1.3	-15.3	-16.4	-13.0
Transportation	-0.4	-3.9	-4.2	-0.4	-5.0	-5.5	-7.0
International travel	-0.4	-2.9	-3.3	-0.1	-5.1	-5.2	-1.5
Computer and informat.	-0.1	-1.9	-2.1	-0.1	-2.4	-2.5	-2.7
Operational leasing	-0.6	-5.3	-5.8	-0.8	-6.6	-7.1	-6.8
Other	0.2	2.1	2.3	0.2	3.7	3.9	5.0
Income	-2.4	-25.9	-29.3	-1.8	-36.7	-40.9	-28.5
Interest	-0.3	-7.0	-7.3	-0.5	-6.5	-7.6	-9.0
Profits and dividends	-2.1	-19.3	-22.4	-1.4	-30.7	-33.7	-20.0
Compensation of employees	0.0	0.4	0.4	0.1	0.5	0.5	0.5
Current transfers	0.3	3.6	4.0	0.4	3.8	4.1	2.5

1/ Forecast.

balance of trade reduction processes and to the acceleration of deficit in services and income accounts, in an environment of net remittances of profits and dividends.

Considering the first eleven months of the year, the deficit reached US$25.8 billion, against surplus of US$2.2 billion in the corresponding period of 2007, a result due to the cutback of 38.3% in the trade surplus and to respective expansions of 28.6% and 41.9% in net remittances of services and income, which summed up, in the order, US$15.3 billion and US$36.7 billion, from January to November 2008.

Revenues from international travel reached US$5.3 billion and expenditures, US$10.3 billion, showing respective expansions of 17.2% and 39% when compared to the first eleven months of the year. Net expenditures totaled US$5.1 billion, a US$2.1 billion increase during the period, a development consistent with growth in available income and with the downward trajectory of the exchange rate until the international crisis intensified. Considering twelve months, up to November, the account registered net outflows of US$5.4 billion, 76.2% higher than the ones registered in the corresponding period of 2007. This result corresponded to a 17.1% growth in revenues and 39.9% in expenditures, which reached, in the same order, US$5.7 billion and US$11.1 billion.

In the year, up to November, an acceleration in net remittances of profits and dividends and a reduction in interest net expenditures were observed. In relation to the first ones, there was a net outflow of US$30.7 billion, representing growth of 59.1% as compared to the same period in 2007, with emphasis on the respective expansions of 55% and 61.9% in gross expenditures with foreign direct and portfolio investments. Considering the twelve-month period ended in November, net revenues of profits and dividends totaled US$33.8 billion, with FDI gross outflows reaching US$26.4 billion, boosted by revenues in the segment. These outflows were directly affected by periods of low profitability in the parent companies abroad or by turmoil in the international financial markets. The remittances in the segments of automotive vehicles, metallurgy and financial services were the more significant and summed up, taken together, US$11.5 billion, representing approximately 50% of outflows from FDI profits and dividends in the first eleven months of 2008.

Net expenditures with interests, consistent with the trajectory of the external indebtedness and with the volume of international reserves, summed up US$6.5 billion in the first eleven months of the year, dropping 7.1% in relation to the corresponding period of 2007. Gross revenues with interests increased 4.2% on the same basis of comparison, a volume compatible with the expansion of Brazilian assets abroad, particularly with regard to growth in international reserves. In that case, earnings grew by 16.7% in the period, reaching US$6.6 billion, while gross payment of interests remained stable. Net expenditures on interests totaled US$6.8 billion in the twelve months ended in November, decreasing 14.6% in relation to the same period of 2007. This result was particularly due to the earnings of US$7.3 billion in international reserves, 21.6% higher than those registered in the corresponding period of 2007.

Net unilateral transfers totaled US$3.8 billion in the first eleven months of the year, increasing 5.5% in relation to the same period of 2007. While considered the twelve months ended in November, these net inflows grew by 7.6%. One should underscore, on the same basis of comparison, the respective decreases of 3.8% and 5.5% observed on the remittances for residents maintenance, accumulating, in order, US$2.1 billion and US$2.2 billion.

5.4 Financial account

Table 5.7 – Financial account

US$ billion

Itemization	2007			2008			2009
	Nov	Jan-Nov	Year	Nov	Jan-Nov	Year[1/]	Year[1/]
Capital account	8.1	84.4	88.2	-6.0	34.9	35.1	42.3
Direct investments	0.1	30.4	27.5	0.5	19.6	23.4	30.0
Abroad	-2.4	-3.3	-7.1	-1.7	-17.3	-17.0	0.0
In Brazil	2.5	33.7	34.6	2.2	36.9	40.0	30.0
Equity capital	2.3	24.8	26.1	1.4	24.1	26.7	30.0
Intercompany loans	0.2	8.9	8.5	0.8	12.8	13.7	0.0
Portfolio investments	-1.2	39.7	48.4	-4.2	5.4	0.1	-7.9
Assets	-0.2	-1.2	0.3	0.3	0.8	0.0	0.0
Liabilities	-1.0	40.9	48.1	-4.5	4.6	0.1	-7.9
Derivatives	-0.1	-0.5	-0.7	0.0	-0.3	0.0	0.0
Other investments	9.3	14.8	13.0	-2.3	10.2	11.6	20.3
Assets	3.6	-19.8	-18.6	0.0	-11.4	-6.3	16.0
Liabilities	5.7	34.7	31.5	-2.3	21.6	17.0	4.2

1/ Forecast.

The balance of payments financial account showed deficit of US$6 billion in November, accumulating surplus of US$34.9 billion in the year. The direct Brazilian investments abroad, evincing the continuity of the Brazilian companies' internationalization process, showed net outflows of US$17.3 billion in the first eleven months of the year, of which US$10.9 billion relates to equity ownership +and US$6.4 billion net granting of intercompany loans.

FDI net inflows summed up US$36.9 billion in the first eleven months of the year, registering net inflows in the capital participation of US$24.1 billion and intercompany loans of US$12.8 billion. FDI net inflows accumulated in twelve months topped US$37.8 billion in November, equivalent to 2.41% of GDP.

In line with the deepening world economic crisis and the consequent mounting uncertainties and risk aversion in the international financial markets, foreign portfolio investments had a deficit of US$4.5 billion in November, totaling net inflows of US$4.6 billion in the first eleven months of the year. From this total foreign investments in stocks of Brazilian companies accounted for net outflows of US$9.9 billion, negotiated in the country. Such investments, after

Table 5.8 – BP financing sources
Selected items

US$ billion

Itemization	2007			2008			2009
	Nov	Jan-Nov	Year	Nov	Jan-Nov	Year 1/	Year 1/
Medium and long-term funds	1.0	22.5	24.3	0.5	12.4	13.2	10.7
Public bonds	0.0	2.9	2.9	0.0	0.5	0.5	0.0
Private debt securities	0.7	14.1	15.4	0.3	6.7	7.3	6.2
Direct loans	0.4	5.5	6.0	0.2	5.2	5.4	4.6
Short-term loans (net) 2/	2.2	17.4	13.8	-2.7	2.1	2.0	0.0
Short-term sec. (net)	0.0	4.6	3.7	-1.2	-0.8	-0.9	0.0
Portfolio (net)	-0.5	35.9	45.1	-2.1	4.9	2.7	-3.0
Roll-over rates (%)							
Private sector:	211%	114%	109%	22%	129%	100%	75%
Debt securit.	187%	233%	186%	21%	106%	79%	75%
Direct loans	273%	49%	52%	25%	180%	154%	75%

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

Table 5.9 – Statement of international reserves

US$ billion

Itemization	2007		2008		2009
	Jan-Nov	Year	Jan-Nov	Year 1/	Year 1/
Reserve position in previous period	85.8	85.8	180.3	180.3	194.1
Net Banco Central purchases	76.3	78.6	0.7	-0.3	12.7
Spot	76.3	78.6	12.4	12.4	-
Repo lines of credit	-	-	-10.2	-7.8	7.8
Foreign currency loans	-	-	-1.5	-4.9	4.9
Debt servicing (net)	-8.4	-7.8	-0.9	-0.5	-0.9
Interest	0.9	1.5	2.3	2.7	1.0
Credit	5.7	6.3	6.6	7.1	5.2
Debit	-4.8	-4.9	-4.3	-4.4	-4.2
Amortization	-9.2	-9.3	-3.2	-3.2	-1.9
Disbursements	2.9	2.9	1.3	1.3	-
Multilateral organizations	-	-	0.8	0.8	-
Sovereign bonds	2.9	2.9	0.5	0.5	-
Others 2/	6.6	6.9	5.7	5.7	-
Treasury's purchases	13.9	14.0	7.5	7.6	6.0
Change in assets	91.2	94.5	14.3	13.8	17.9
Gross reserve position	177.1	180.3	194.7	194.1	212.0
Repo lines of credit position	-	-	10.2	7.8	-
Foreign currency loans position	-	-	1.5	4.9	-
Reserves position - liquidity	177.1	180.3	206.4	206.8	212.0

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.

registering significant net inflows from March to May, have been showing net remittances since June. The net revenues in the segment of fixed- income securities negotiated in the country topped US$14.8 billion in the year. One should note that these flows, evincing the financial markets deterioration, showed net outflows of US$1.7 billion in October and of US$300 million in November.

Foreign investments on fixed-income securities, negotiated abroad, showed net amortizations of US$3.6 billion in the first eleven months of 2008. With regard to the National Treasury repurchase program, the medium- and long-term bonds, net amortizations totaled $3.5 billion, of which US$3.2 billion refer to face value of securities, and US$290 million to premiums of these operations.

Net amortizations of medium- and long-term private bonds reached US$1.2 billion in November, accumulating net disbursements of US$138 million in the first eleven months of the year, a period in which the short-term securities showed net amortizations of US$756 million.

Other Brazilian investments registered net outflows of US$8 million, in November, for an increase of assets abroad of US$11.4 billion, in the year, a result of the constitution of deposits of Brazilian banks abroad, US$4 billion, and deposits of other sectors abroad, US$4.9 billion, besides the net granting of US$3.9 billion of medium- and long-term loans to nonresidents.

Other foreign investments showed net outflows of US$2.3 billion in November, accumulating net inflows of US$21.6 billion in the year. When braking down this result, the short-term trade credit accounted for net inflows of US$807 million in the month and US$8.3 billion in the first eleven months of the year. Medium and long-term loans summed up net amortizations of US$389 million in November and net disbursements of US$12.2 billion in the year, while short-term loans registered net outflows of US$2.7 billion and net disbursements of US$2.1 billion in the year.

The impact of the reversal in the international economic outlook on the credit channels led the Central Bank to act on the exchange market aiming at adjusting the liquidity conditions in foreign currency. In this context, sales intervention on the spot market totaled US$1.7 billion in November. However, there was no sign of any modification in the monetary authority stance of not acting upon the trajectory nor defining floors or ceilings for the nominal

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

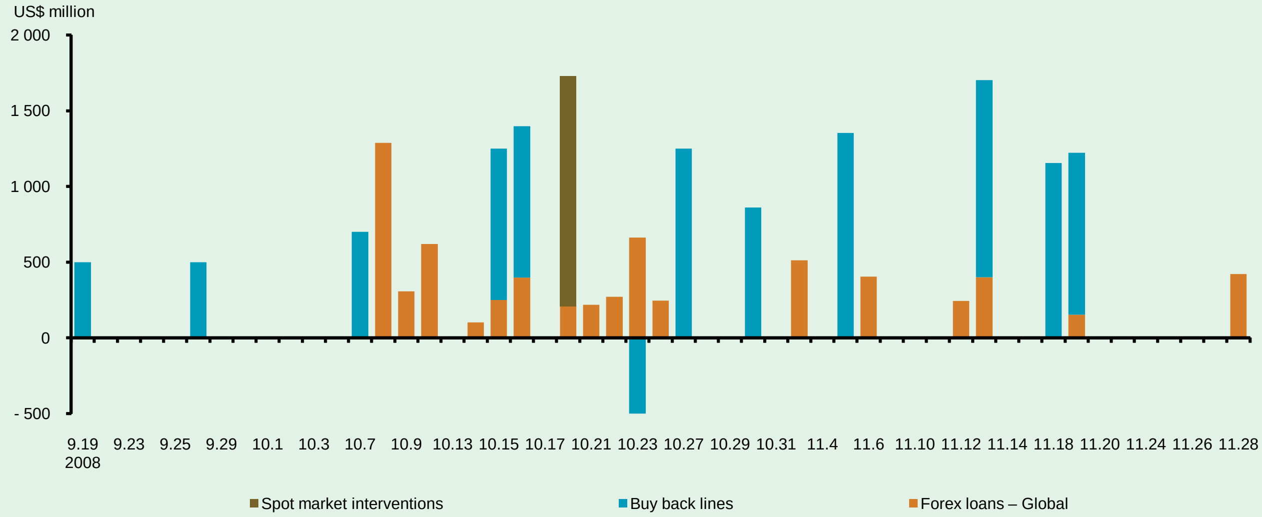
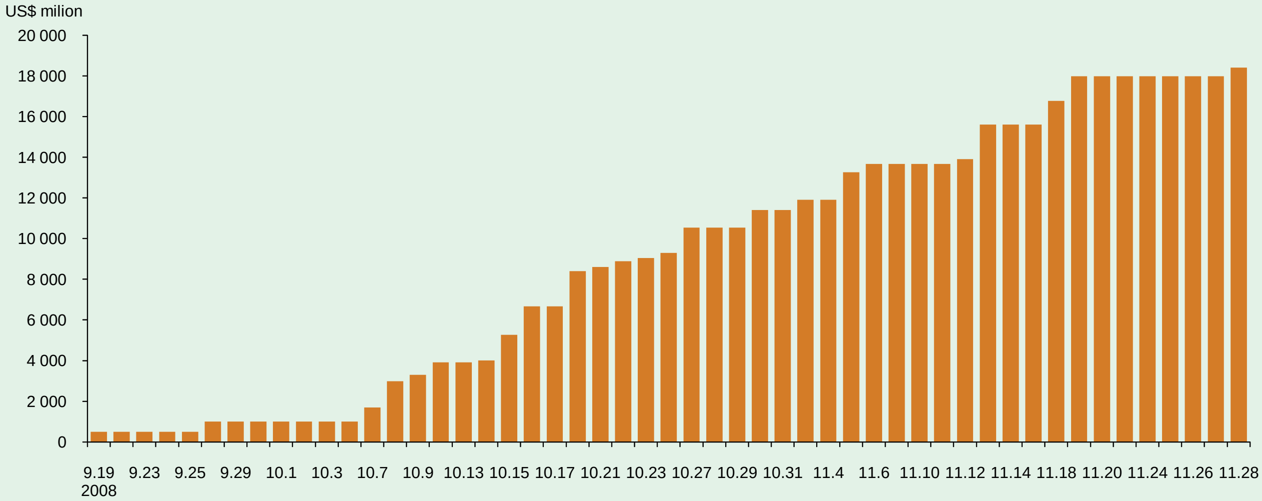


Figure 2 – Measures aiming at Forex Liquity (cumulative)



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	Value
	Loan	Amortization			bids	US$ million
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	Value
	Loan	Amortization			bids	US$ million
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
	Sale	Purchase		US$ million
9.19.2008	9.23.2008	10.23.2008	30	500
9.26.2008	9.30.2008	12.19.2008	80	500
10.7.2008	10.9.2008	1.7.2009	90	700
10.15.2008	10.17.2008	1.15.2009	90	1 000
10.16.2008	10.20.2008	4.20.2009	182	1 000
10.27.2008	10.29.2008	1.2.2009	65	750
10.27.2008	10.29.2008	2.2.2009	96	500
10.30.2008	11.3.2008	2.2.2009	91	860
11.5.2008	11.7.2008	12.8.2008	31	1 353
11.13.2008	11.17.2008	12.17.2008	30	1 302
11.18.2008	11.20.2008	12.19.2008	29	1 155
11.19.2008	11.21.2008	1.2.2009	42	110
11.19.2008	11.21.2008	2.2.2009	73	130
11.19.2008	11.21.2008	3.2.2009	101	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 irretraceable 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)

foreign rate of exchange. Besides, new credit modalities were announced in particular those involved in offering new credit lines to the banking sector. The Central Bank started to sell dollars with repurchase commitment, a modality which summed up amortizations of US$1 billion in September, US$3.5 billion in October and US$5.7 billion in November. Additionally, foreign currency loans were granted against guaranties. In that case, resources should be fully targeted to export financing. The first auction, backed by Brazilian sovereign bondses, topped US$1.5 billion. In November, there were three auctions, in which loan granting guaranteed by external trade operations, which totaled net US$3.4 billion, in December.

With regard to the stock of the previously described new operations, the international reserves, in the liquidity concept, grew US$26 billion in the period from January to November 2008, totaling US$206.4 billion. The Central Bank carried out net purchases of US$691 million in the foreign exchange domestic market. Among the external operations, it should be highlighted the US$525 million disbursements in Republic bonds and US$766 million from the International Bank for Reconstruction and Development (Bird), besides US$3.2 billion amortizations of sovereign bonds, including, in the latter case, US$1.1 billion related to operations to repurchase external debt's securities by the National Treasury. The expenditures with bonds interests summed up US$4.3 billion, while the revenue with the reserves' earnings reached US$6.6 billion, turning in interest-related net revenues of US$2.3 billion. The National Treasury's purchases amortizations totaled US$7.5 billion, while other operations resulted in revenues of US$5.7 billion.

At the closing of 2008, international reserves stock, in the liquidity concept, are estimated at US$206.8 billion, with an annual growth of US$26.5 billion. Regarding the events from January to November, payments related to the external debt service are forecasted at US$0.5 billion, besides disbursements of US$766 million already fully settled with organizations, and of those related to sovereign bonds, US$525 million. Also, it is estimated, Central Bank' sale settlements of US$308 million and the National Treasury purchases of US$7.8 billion of the, on the foreign exchange domestic market.

International reserves in the cash concept, which excludes operations with repurchase lines and foreign currency loans, should close 2008 at US$194.1 billion, rising US$13.8 billion as compared to the end of 2007. The difference between the reserves value in the two concepts indicates the end-of-period stocks of repurchase lines, US$7.8 billion, and foreign currency loans, US$4.9 billion, included in the liquidity concept.

For 2009, a stock of international reserves is estimated, in the liquidity concept, at US$212 billion, with annual growth of US$17.9 billion. Net expenditures are anticipated at US$858 million with the external debt service, comprising US$1 billion in net interest 0revenues and US$1.9 billion in amortization expenditures. Still in 2009, purchase amortizations by the National Treasury on the foreign exchange domestic market, are forecasted at US$6 billion. It important to stress that the repurchase of the credit lines available to the market and foreign currency loan maturities will enable the reserves in both cash and liquidity concepts to reach a balanced position by end of 2009.

5.5 External sustainability indicators

Despite the reversal in the international outlook initiated halfway through the second half-year, the majority of the external sustainability indicators turned in a a positive trajectory, when considering the estimated external debt positions for November and December 2007. This movement indicated both growth in exports, dollar denominated nominal GDP and international reserves, and the reduction of the external debt service, as well as improved surplus positions of the total net external debt. In that case the effects have proved to be more significant than that derived from the expansion of the external debt.

In the period under analysis, the participation of the debt service in exports dropped from 32.4% to 18.8%, indicating a cutback of US$14.7 billion in the debt service and an increase of US$37.7 billion in sales to other countries.

The total external debt increased 6.9% from December 2007 to November 2008, while the total surplus position of the net external debt grew US$13.3 billion, to –US$25.2 billion. Taking into account the growth of 18% observed in the estimated GDP in dollars during the period, the ratios between the total debt/GDP, and the total net debt /GDP decreased from 14.5% to 13.2% and from 0.9% to -1.6% in that order.

The indicator showing the ratio between the total debt and exports decreased from 1.2 to 1, while that which indicates the proportion between the net total debt and the exports

Table 5.10 – Sustainability indicators[1/]

US$ billion

Itemization	2006	2007	2008			
	Dec	Dec	Jun	Sep	Oct[2/]	Nov[2/]
Exports of goods	137.8	160.6	178.1	194.9	197.7	198.4
Exports of goods and services	157.3	184.5	205.0	224.2	227.7	228.4
Debt service	56.9	52.0	40.5	38.9	36.4	37.4
Total external debt	172.6	193.2	205.5	211.4	214.3	206.6
Net external debt	74.8	-11.9	-19.2	-20.6	-13.4	-25.2
International reserves						
Cash concept	85.8	180.3	200.8	206.5	197.2	194.7
Liquidity concept	85.8	180.3	200.8	206.5	203.2	206.4
GDP	1 089	1 334	1 461	1 530	1 550	1 569
Indicators						
Total external debt/GDP (%)	15.8	14.5	14.1	13.8	13.8	13.2
Net external debt/GDP (%)	6.9	-0.9	-1.3	-1.3	-0.9	-1.6
Total external debt/exports	1.3	1.2	1.2	1.1	1.1	1.0
Total external debt/exports of goods and services	1.1	1.0	1.0	0.9	0.9	0.9
Net external debt/exports	0.5	-0.1	-0.1	-0.1	-0.1	-0.1
Net external debt/exports of goods and services	0.5	-0.1	-0.1	-0.1	-0.1	-0.1
Debt service/exports (%)	41.3	32.4	22.8	19.9	18.4	18.8
Debt service/exports of goods and services (%)	36.2	28.2	19.8	17.3	16.0	16.4
Reserves – cash concept/ total external debt (%)	49.7	93.3	97.7	97.7	92.0	94.2
Reserves – liquidity concept/ total external debt (%)	49.7	93.3	97.7	97.7	94.8	99.9

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

Recent Changes in Brazil's External Liabilities

The country's external accounts registered a sequence of five years of surplus in current transactions between 2003 and 2007, enabling the occurrence of strong expansion of Brazilian assets abroad, which increased from US$112.9 billion, up to the end of 2002, to US$369.7 billion in 2007 and to an estimated US$418.2 billion, in October 2008. Contrary to the expectations of reduced net external liabilities as counterpart to the current account results, an increase was observed in the period, in line with the price trajectory of the external liabilities and the foreign exchange rate. This box analyzes the evolution and modifications to the Brazilian external liabilities in the latest years, in a context of non-resident investments' expansion, both in portfolio and direct; reduction of the external debt's relative participation; and greater adherence of this new liabilities composition to the domestic economic cycle.

The country's gross external liabilities posted a steady growth from 2003 to June 2008, in a backdrop of faster economic growth sustained by domestic demand, increase of the corporate profitability, and the capital market's favorable development. These factors contributed to an increasing capital inflow in the period.

Up to the end of 2008, the International Investment Position (IIP) liabilities reached the highest value of US$1,060 billion, representing an increase of 208.7% as compared to December 2002. The foreign direct investments (FDI), which turned in a growing inflow during the period, registered an annual record of US$34.6 billion in 2007, a value which should be surpassed in 2008, despite the international economic crisis. In view of the behavior of net flows and nominal foreign exchange, taking into account that the stocks of FDI-equity participation in the country are measured in Reais, the FDI forecasted position for June 2008 topped US$381.2 billion, which is 36% of the IIP total liabilities.

Table 1 – International Investment position – Liabilities

US$ million

Itemization	2001	2002	2003	2004	2005	2006	2007	2008	
	Dec	Dec	Dec	Dec	Dec	Dec	Dec	Jun	Oct
Liabilities (B)	**372 061**	**343 432**	**406 716**	**446 145**	**499 268**	**623 300**	**939 071**	**1 060 019**	**755 668**
Foreign direct investment	121 948	100 863	132 818	161 259	195 562	236 186	328 455	381 184	317 595
Equity capital	105 815	83 884	112 334	142 451	177 024	209 403	281 179	324 291	254 179
Intercompany loans	16 133	16 978	20 484	18 808	18 537	26 783	47 276	56 893	63 416
Portfolio investiments	151 741	137 355	166 095	184 758	232 627	303 583	509 648	565 018	313 847
Stock investiments	36 910	27 249	53 138	77 261	125 532	191 513	363 999	402 069	172 871
In the reporting company	13 386	8 394	17 828	27 118	50 394	82 994	165 708	194 214	76 064
Abroad	23 524	18 855	35 310	50 143	75 138	108 520	198 291	207 855	96 807
Fixed-rate securities	114 831	110 106	112 957	107 497	107 096	112 070	145 650	162 949	140 977
Bonuses and notes	114 831	110 106	112 957	107 497	107 096	112 070	145 650	162 949	140 977
In the reporting company	1 642	2 492	2 867	2 982	5 147	18 163	46 631	63 552	44 601
Abroad	113 189	107 614	110 090	104 515	101 949	93 907	99 018	99 397	96 376
Medium- and long-term	111 989	106 614	108 476	104 271	101 047	92 119	93 079	93 348	89 332
Short-term	1 200	1 000	1 614	244	901	1 788	5 939	6 050	7 043
Derivatives	45	250	125	320	219	445	1 771	2 510	3 425
Other investments	98 327	104 965	107 678	99 809	70 859	83 087	99 197	111 307	120 800
Commercial credit (suppliers')	6 025	5 919	5 465	4 728	4 772	5 216	5 197	6 373	6 323
Medim- and long-term	5 398	4 896	5 037	4 414	4 424	4 869	5 063	6 161	5 964
Short-term	628	1 023	428	314	349	347	134	213	359
Loans	90 720	97 178	99 374	92 133	62 729	73 466	89 003	99 766	109 462
Monetary authority	9 130	21 457	28 795	25 394	301	157	14	12	9
IMF	8 346	20 793	28 255	24 946	-	-	-	-	-
Other long-term loans	784	664	540	448	301	157	14	12	9
Short-term	-	-	-	-	-	-	-	-	-
Other sectors	81 590	75 721	70 579	66 739	62 428	73 309	88 989	99 754	109 453
Medium- and long-term	55 759	54 348	52 427	48 553	44 902	55 121	56 162	64 740	68 454
Organizations	22 440	24 377	23 433	22 241	21 779	25 148	26 981	28 335	29 419
Offices	12 418	12 731	12 856	10 970	8 614	6 259	6 482	6 505	6 486
Buyer's credit	8 362	6 317	6 542	4 984	4 059	3 707	8 232	12 748	15 098
Direct loans	12 539	10 924	9 596	10 358	10 449	20 007	14 467	17 152	17 451
Short-term	25 831	21 373	18 152	18 186	17 527	18 188	32 827	35 014	40 999
Currency and deposits	1 582	1 867	2 839	2 948	3 358	4 405	4 996	5 168	5 014
Monetray Authority	129	237	108	100	111	83	73	54	67
Banks	1 453	1 630	2 731	2 848	3 246	4 321	4 923	5 114	4 947
Other liabilities	-	-	-	-	-	-	-	-	-

In relation to foreign portfolio investments, one should highlight the growth of investments on securities and on the country's fixed-income securities. The inflows in securities, considering both the participation of non-resident investors in the Bovespa, and the issue of receipts of Brazilian companies' shares on the international market, reaching a stock of US$402.1 billion, in June 2008, which corresponds to 37.9% of total liabilities, an evolution impacted by net inflows, by appreciation of papers and by the evolution of foreign exchange rate. As to foreign investments in fixed-income bonds negotiated in the country, one should highlight the exemption of income tax, instituted by Provisional Measure 281, of February 15, 2006, later turned into Law 11.312. This measure accelerated the net inflows, resulting in stock of US$63.6 billion, in June 2008.

On the other hand, the liabilities items which represented the external debt, mainly papers negotiated in the international market and borrowings, showed nominal reduction of 2.5% during the period from December 2002 to June 2008, which totaled US$205.5 billion. In this way, its relative participation in the total IIP liabilities reduced from 61.4% to 19.4%, in the period.

With the modification in the profile of the Brazilian external liabilities, not only the stock of liabilities, but also its revenues started to show a behavior more associated to the economic cycle. This modification mirrored the replacement of contractual debts, which has its stocks calculated in nominal values and whose payment conditions are preset, by investments, for which both the stock valuation and its remuneration (earnings and dividends) are estimated at market prices.

This change in the external liabilities' behavior may be better assessed when compared to the stocks of last June, prior to the intensification of the international financial crisis, with the estimates made for this position in October. The position of liabilities of the IIP at the end of this month, as compared to the one observed in June; fell by 28.7% to US$755.7 billion. In that same period, there were differentiated trajectories among investments, with reduction in stocks of FDI- equity participation, securities and fixed-income securities negotiated in the country, and external indebtedness, with expansion of its stock.

The main factor responsible for the contraction in liabilities was the stock reduction of by foreign investors in stock in the country, which, according

Table 2 – Stocks in the country

	US$ million
Stock in 6.30.2008	194 214
Balance of payment's cumulative net flows	
from July to October	-13 351
Ibovespa variation from 6.30.2008 to 10.31.2008	-66 100
Exchange rate variation from 6.30.2008 to 10.31.2009	-30 700
Remainder	-7 999
Stock in 10.31.2008	76 064

to the Securities and Exchange Commission (CVM), topped US$76.1 billion in October, falling no less than 60.8% as against June. Analyzing the factors responsible for this trajectory, it was observed, in the period, net outflows of US$13.4 billion and reduction in market value (price) and in the value of this stock in dollars (parities). The assessment of price reduction was made using as a parameter the São Paulo Stock Exchange Index (Ibovespa) which, in the period, decreased 42.7% causing an estimated reduction in the stock of US$66.1 billion. The expression of these liabilities in dollars is directly impacted by the nominal foreign exchange rate, of which the depreciation of 32.9% in the four-month-period under analysis caused an estimated decrease of US$30.7 billion in the total liabilities. The difference of US$8 billion derives from changes of the foreign investor's instrument in the country and from the difference between the real portfolio of these investors and the utilization of the Ibovespa as proxy.

Growth in FDI-equity participation in the capital and of fixed-income securities negotiated in the country, whose positions are calculated in nominal values and in reais, is conditioned by net flows of the balance of payments and, similar to the way previously described, by the variation of the foreign exchange rate.

The external liabilities cyclical component should also be highlighted when incomes derived thereof are analyzed, especially gross remittances of profits and dividends. As analyzed in the box "Remittances of Profits and Dividends'' of the September 2008 Inflation Report, these remittances show close relation to the stock of foreign investors, both in participation in the capital and securities, and with these companies' earnings, which may be understood as proxy to the domestic activity level. Consequently, the stock reduction, analyzed in this box, should provide, in the next year, retraction in the remittances of profits and dividends, a trajectory stimulated by a lower level of economic activity and by the maintenance of the foreign interest rate at a more depreciated level than the one observed during this year. This analysis strengthens the forecast of significant decrease in net outflows of profits and dividends in 2009, which consists in an important move towards limiting the current transactions deficit next year.

In the same way, the drop of 60.8% in total investments in securities owned by non-residents represents an important limiting factor for portfolio net remittances in the balance of payments’ financial account next year, even if the adverse international scenario is maintained.

remained at -0.1. Both equally represented the most positive results registered since the beginning of the series, in 1970.

In the liquidity concept, the international reserves, increased by US$26 billion from December 2007 to November 2008, reaching US$206.4 billion, while in the cash concept, the expansion totaled US$14.3 billion, up to US$194.7 billion. The expansion of the international reserves in the liquidity concept, higher than the amount of US$13.4 billion registered in the total external debt, favored its representation in the total external debt from 6.6 p.p., to 99.9%. At the same time, those concerning the reserves in the cash concept reached 94.2%, increasing 0.9 p.p., in the period.

The the total net debt/GDP ratio rose to 1.6%, in November, against the creditor position of 0.9% in December 2007, and still recorded a 0.7 p.p. growth when compared to the previous month. The indicator monthly growth represented an increase from US$11.8 billion, to US$25.2 billion, registered in the creditor position of the total net external debt. This was a result of a US$3.2 billion growth in international reserves, in the liquidity concept, and of US$1 billion in commercial banks' assets abroad, as well as the US$7.7 billion decline in the external debt.

5.6 Conclusion

Uncertainties regarding the international financial market's performance, in parallel to the recession prospects for the world economy, particularly in the industrialized countries, the developments in the trajectory of international trade and commodity international prices are major conditioning factors of the growing country's external accounts.

The performance of the external accounts in the initial eleven months of the year suggests that the balance of payments' financing will take place with no difficulty in 2008. This result has been favored by the FDI net inflows, which should surpass the ones registered in 2007, and by the rollover of the private debt, which, in view of what occurred from January to November, should remain above 100%.

Forecasts for 2009 consider that the external credit restriction and the downturn in the pace of international economic activity should cause the deterioration of the balance of payments' result. Satisfactory conditions, however, should persist, for its financing, favored by the level of international reserves and by the advances on contracts made by the National Treasury, which significantly reduce risks concerning amortization of the external debt service. The private sector will face more adverse conditions for the renegotiation of loans in relation to those existing in the latest five years, with negative impacts on the contracting terms and costs.

The reversal recorded in the balance of payments financing need in 2008, was conditioned by the current transactions performance in the year. For 2009, in an environment of slowing world economic activity and greater restriction to credit granting, the current result will be impacted, in the context of the balance of trade by a likely decrease in exports and imports. In the case of exports, the reach will be dependent on the behavior of commodity prices and on the magnitude and extension of the economic downturn in the major markets of destination of Brazilian products. In the case of imports, they evince both price increases underlying the depreciation of the real, and a slowdown in domestic activity. Concerning the service account, the debt under transportation should drop, in line with the reduction in the trade flow; the negative balance in international travel should register a significant decline, mirroring both foreign exchange trade trajectory and the wealth effect on these expenditures. Net expenses on earnings will be affected by the expected decline in net remittances of profits and dividends and by the combined effects of a depreciated foreign exchange rate, lower profitability of companies and foreign investors losses in variable income, which indicate a reduced stock of investments.

Balance of Payments Forecasts

The balance of payments forecasts for 2008 and 2009 were revised in relation to those in the September Inflation Report. This was due to the repercussions of a deepening crisis of the financial markets both in terms of world economic activity level, impacting the balance of payments result, and of liquidity conditions, affecting the prospects concerning its financing conditions. Besides incorporating the new international outlook, revised forecasts mirror the external results observed in the latest months and the modifications in the external debt service compatible with its stock in September. Additionally, Central Bank interventions in the foreign exchange market and repurchases of sovereign external debt by the National Treasury, carried out up to November.

The current transactions deficit in 2008 was revised upward from US$28.8 billion, in the previous "Inflation Report", to US$29.6 billion. One should also highlight the revision of the trade surplus forecast, from US$25 billion to US$23.5 billion. Additionally, the forecasts for net expenditures with interest and international travel were reduced.

Forecasts for the debt in current transactions in 2009 were reduced from US$33.1 billion to US$25 billion.

The balance of trade surplus reflected a 3.5% decrease in exports and a 1.4% growth in imports, dropping from US$23.5 billion, in 2008, to US$14 billion, a forecast US$3 billion lower than that indicated in the previous report and consistent with the expectations of recession in mature economies, reduction in commodity prices and decline in the Gross Domestic Product (GDP).

Forecasts for net interest expenditures next year expanded from US$6.7 billion, in the previous

Table 1 – Uses and sources

US$ billion

	2007			2008			2009
	Nov	Jan-Nov	Year	Nov	Jan-Nov	Year1/	Year1/
Uses	-3.3	-33.1	-36.6	-3.9	-45.1	-53.0	-51.9
Current account	-1.3	1.9	1.5	-1.0	-25.8	-29.6	-25.0
Amortizations ML-term2/	-2.0	-35.0	-38.1	-2.9	-19.3	-23.3	-26.9
Securities	-1.1	-18.1	-20.6	-1.6	-10.0	-12.8	-11.1
Paid	-1.1	-17.6	-19.9	-1.6	-10.0	-12.8	-11.1
FDI conversions	0.0	-0.5	-0.7	0.0	0.0	0.0	0.0
Suppliers' credits	-0.2	-1.3	-1.5	-0.2	-1.6	-1.7	-3.1
Direct loans3/	-0.7	-15.5	-16.1	-1.1	-7.7	-8.8	-12.7
Sources	3.3	33.1	36.6	3.9	45.1	53.0	51.9
Capital account	0.1	0.7	0.8	0.1	1.0	1.1	1.0
FDI	2.5	33.7	34.6	2.2	36.9	40.0	30.0
Domestic securities4/	-0.5	31.0	39.8	-2.0	6.8	5.5	-3.0
ML-term disbursem.5/	3.8	32.9	36.0	1.2	29.2	30.8	26.5
Securities	0.7	17.0	18.3	0.3	7.2	7.8	6.2
Supliers' credits	0.2	1.4	1.6	0.1	2.1	2.4	4.1
Loans6/	2.9	14.5	16.1	0.7	19.9	20.5	16.3
Brazilian assets abroad	0.9	-24.3	-25.4	-1.3	-27.7	-22.9	15.2
Other7/	2.9	43.4	38.4	-3.1	7.3	6.1	0.0
Reserve assets	-6.4	-84.4	-87.5	6.8	-8.5	-7.5	-17.9

1/ Forecast.
2/ Registers amortization of medium and long-term suppliers' credit, loans and securities placed abroad minus refinancing and discounts. Excludes amortization referring to loans to IMF and intercompany loans.
3/ Registers amortizations of loans from foreign banks, buyers, bilateral agencies and multilateral organizations.
4/ Includes foreign investment in equity and debt securities traded in the domestic market.
5/ Excludes disbursements of intercompany loans.
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, deposits of non-residents, other liabilites and errors & omissions.

report, to US$9 billion, mirroring the decrease, from US$9.1 billion to US$7.1 billion – of which US$5.2 billion refer to interest earning on the country's international reserves, on interest revenues over Brazilian assets abroad, a decrease that evinces the decline in the international interest rates and the reduction of these assets. The expenditures, translating the debt stock position in September, fell from US$17.6 billion to US$16.1 billion.

Forecasts for the result in current transactions for 2009 considers the revision, from US$30 billion to US$20 billion, in the estimate concerning net remittances of profits and dividends, a drop consistent with the scenario of depreciation of the real, reduction of companies' profitability and strong losses experienced by foreign portfolio investors, which are mirrored in the reduction of the investment stock. In this context, one should mention that the position of foreign investors at the São Paulo Stock Exchange Index (Ibovespa) fell from US$200.1 billion in May to US$70.6 billion at the end of November. The unilateral transfers for 2009 were lowered from US$4 billion, forecasted in September, to US$2.5 billion, as a result of the recession in mature economies, main suppliers of these resources.

The performance of the financial account in the next year mirrors a scenario which considers reduction of the net inflows of Foreign Direct Investments (FDI). Additionally, it is forecasted net remittances of foreign portfolio investments in 2009. Also significant to these scenarios the assumption of 75% rollover rate of the medium- and long-term private sector external indebtedness leading to a net amortization of the external debt.

The internationalization process of the Brazilian companies should be impacted by the international crisis's effects. In this context, there will not be net remittances of Brazilian direct investments abroad, and after registering the record level of US$28.2 billion, in 2006, the stock should remain stable in 2009. Foreign direct investments should total US$40 billion in 2008; a record for annual values. For 2009, the forecast was reduced to US$30 billion.

The external debt amortizations of medium- and long-term in 2008 were reduced from US$25.7 billion

Table 2 – Balance of payments – Market

US$ billion

Itemization	2007 Oct	2007 Jan-Oct	2007 Year	2008 Oct	2008 Jan-Oct	2008 Year[1/]	2009 Year[1/]
Current account	-1.9	-2.7	-4.6	-1.6	-32.4	-36.1	-30.2
Capital (net)	5.7	89.6	93.9	-6.6	37.0	32.2	26.8
Foreign direct investment	2.5	33.7	34.6	2.2	36.9	40.0	30.0
Portfolio investment	-0.5	31.0	39.8	-2.0	6.8	5.5	-3.0
Med. and long term loans	0.4	-9.2	-9.9	-1.8	2.7	-0.7	-4.9
Trade credits – Short, medium and long term	5.2	39.4	35.8	-1.8	17.1	16.9	4.6
Banks	3.5	21.7	18.6	-2.6	8.2	11.7	3.6
Other	1.8	17.8	17.2	0.7	8.8	5.2	1.0
Brazilian invest. abroad	-1.0	-14.4	-14.7	-2.0	-23.7	-26.5	-0.9
Other	-1.1	9.1	8.3	-1.2	-2.7	-3.0	1.0
Financial gap	3.8	86.2	89.3	-8.2	4.6	-3.9	-3.4
Banco Central net interv.	-5.7	-76.3	-78.6	7.5	-0.7	0.3	-12.7
Bank deposits	1.9	-9.9	-10.7	0.7	-4.0	3.6	16.1

1/ Forecast.

to US$23.3 billion. For 2009, the forecast was revised to US$26.9 billion. Additionally, the assumption of rollover rates for the external indebtedness was reduced from 100% to, as already mentioned, 75%, showing net amortization of external loans.

The forecast for 2008, related to foreign investment net inflows of medium- and long-term domestic securities was reduced, significantly, from US$22 billion, in the September Inflation Report, to US$5.5 billion, in line with the results recently registered and with the assumption of maintenance of the financial stress scenario. For 2009, in line with the prospects of persistent risk aversion and of maintenance of the other macroeconomic conditions, these net flows were revised from net inflow of US$15 billon to net outflow of US$3 billion.

The banking sector's assets abroad should decrease by US$3.6 billion in 2008, against US$0.6 billion forecasted in the September Inflation Report, having as forecasted, for 2009, returns of US$16.1 billion, as compared to US$7.4 billion in the previous forecast. The reduction of the banking sector's assets abroad shows the behavior of the foreign direct and portfolio investments and of the forecasted balance for the current transactions, evincing the banking sector's performance as foreign currency supplier to the non-financial private sector.

Regarding the international reserves, considering the liquidity concept, their position up to the end of 2008 should show growth of US$26.5 billion as compared to the previous year, topping US$206.8 billion. For 2009, it is forecasted an additional expansion of US$5.2 billion as a result of the reserve earnings, with additional interventions not being forecasted. Considering the international reserves, in the cash concept, which incorporates the effects of the recent measures adopted by the Central Bank to supply liquidity in foreign currency, the reserves continue to turn in expansion in the year. The forecast presented in this Inflation Report shows the international reserves, in the cash concept, at US$194.1 billion, to the end of 2008, expansion of US$13.8 billion in relation to 2007. Towards the end of the following year, already repurchased all the lines and foreign currency loans, both concepts will even, reaching US$212 billion.