Credit, monetary and fiscal policies

3

3.1 Credit

The expansion of financial system credit transactions in the quarter ended October reflected a persistent economic activity dynamics and the seasonal impact of the end of year sales. Financing granted with earmarked funds continued to be more robust, especially transactions contracted with the BNDES and housing financing. As for the nonearmarked credit portfolio, it is worth mentioning the performance of car loans.

The stock of financial system credit transactions totaled R$1,645 billion in October 2010, increasing 6.3% in the quarter and 20.3% in twelve months, representing 47.2% of GDP, compared to 45.5% in July and 44.6% in the same period of the previous year. The participation of public banks in total credit operations reached 41.9%, against 42.2% in July and 40.7% in the same period of 2009, whereas the share of private national institutions and foreign banks reached 40.6% and 17.5%, respectively, compared to 40.1% and 17.6% in July, and 40.6% and 18.7% in the same period of 2009.

Credit to the private sector totaled R$1,578 billion in October, accounting for 96% of the national financial system total credit operations, for a 6.5% increase in the quarter and 20.3% in twelve months. It should be highlighted that the quarterly change reflected, in particular, the increase of 7.7% in the industrial segment. Housing credit transactions, which exerts an important effect on the performance of the construction sector, increased 11.2% in the quarter and 51.5% in twelve months. Of the stock of R$129.1 billion registered in October, 94.8% referred to transactions with savings deposits and the Employment Compensation Fund (FGTS).

The balance of the public sector financing reached R$66.4 billion, increasing 1.7% in the quarter and 19.6% in twelve months, with emphasis on the respective expansions of 5.3% and 37.7% on the regional level.

Table 3.1 – Credit operations

R$ billion

Itemization	2010				% growth	
	Jul	Aug	Sep	Oct	3 months	12 months
Total	1 547.9	1 584.5	1 613.6	1 644.8	6.3	20.3
Nonearmarked	1 025.0	1 042.2	1 061.6	1 078.9	5.3	15.7
Earmarked	523.0	542.2	552.0	565.9	8.2	30.0
% participation:						
Total/ GDP	45.5	46.2	46.7	47.2		
Nonearmarked/ GDP	30.1	30.4	30.7	31.0		
Earmarked/GDP	15.4	15.8	16.0	16.3		

Figure 3.1 – Credit by capital control of financial institutions

% of balance

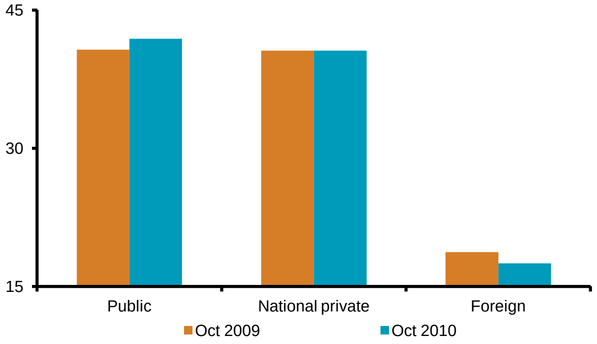
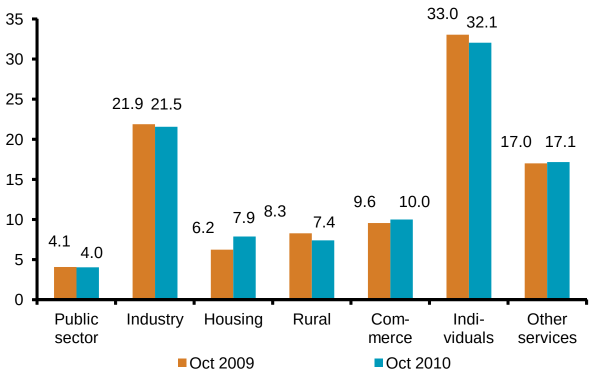


Figure 3.2 – Credit by borrower's economic activity

%



Provisions set aside by the financial system totaled R$96.4 billion in October, for respective changes of 1.1% in the quarter and -2.7% in twelve months. The ratio between the amounts set aside and the total credit portfolio reached 5.9%, compared to 6.2% in July, whilst the total financial system default, based on those transactions overdue by more than ninety days, fell 0.2 p.p. in the period, to 3.4%.

With the goal to strengthen prudential regulation and the sustainability of the credit market, the Circular no. 3,515, dated December 3, outlined the increase in capital requirements applicable to credit transactions and commercial lease financing to individuals where the contractual terms exceed 24 months. Accordingly, the Risk Weighting Factor (FPR) for transactions entered into from December 6, 2010 went from 100% to 150%, representing an increase from 11% to 16.5% in the capital requirement. This increase does not apply to the following transactions: i) payroll-deducted loans with contractual period lower than 36 months; ii) rural credit; iii) housing credit; iv) financing or commercial leasing of vehicles with terms between 24 and 36 months, provided that the contract value does not exceed 80% of the vehicle value; v) financing or commercial leasing of vehicles with terms between 36 and 48 months, providing that the contract value does not exceed 70% of the vehicle value; vi) Financing or commercial leasing of vehicles with terms between 48 and 60 months, providing that the contract value does not exceed 60% of the vehicle value; vii) financing or commercial leasing of haulage vehicles; and viii) financing with funds derived from Federal Government funding transfers or special programs.

Earmarked credit

Earmarked credit operations totaled R$565.9 billion in the quarter ended October, rising 8.2% in relation to July and 30% in twelve months, with emphasis on the trajectories of BNDES transactions and housing financing, which registered, on the same comparison basis, respective increases of 7.6% and 10.9%, and 32.4% and 51.1%.

BNDES disbursements reached R$140.9 billion in the first ten months of the year, up 32.3% in comparison to the same period in 2009. Financing to industry, driven by demand from the segments of food and coke, oil and fuel, rose by 33%, while that granted for the segments of trade and services increased 29.6%, with emphasis on the branches of land transportation and trade. Financing to micro, small and medium enterprises, representing 26.4% of total disbursements, grew 105% on the same comparison basis.

Table 3.2 – Earmarked credit operations

R$ billion

	2010				% growth	
	Jul	Aug	Sep	Oct	3 months	12 months
Total	523.0	542.2	552.0	565.9	8.2	30.0
BNDES	322.3	334.9	337.8	347.0	7.6	32.4
Direct	168.9	172.1	171.2	175.2	3.7	20.2
Onlendings	153.4	162.8	166.7	171.8	12.0	47.7
Rural	78.4	80.1	82.3	83.6	6.7	1.9
Banks and agencies	74.6	75.8	77.8	78.9	5.8	1.1
Credit unions	3.8	4.3	4.4	4.7	24.3	17.7
Housing	110.4	114.7	119.0	122.5	10.9	51.1
Others	11.9	12.4	12.9	12.8	7.8	27.5

Table 3.3 – BNDES disbursements

R$ million

	Jan-Oct		
	2009	2010[1/]	% growth
Total	106 486	140 921	32.3
Industry	52 572	69 908	33.0
Mining	1 960	1 183	-39.6
Food products	4 312	11 258	161.1
Vehicle, towing truck and wagon	5 678	5 207	-8.3
Petroleum and alcohol refining	22 519	27 884	23.8
Cellulose and paper	3 228	1 397	-56.7
Transportation equipment	2 403	3 128	30.2
Commerce/services	48 522	62 904	29.6
Overland transportation	19 003	23 326	22.7
Electricity and gas	10 672	9 749	-8.6
Commerce	3 990	8 638	116.5
Auxiliary transportation activities	1 828	2 673	46.2
Construction	4 743	5 339	12.6
Telecommunication	1 992	1 981	-0.5
Crop and livestock	5 393	8 110	50.4

Source: BNDES

Consultations with the BNDES, a leading indicator of productive sector investments, totaled R$224 billion in the first ten months of the year, increasing 21.3% compared to the same period of the previous year, highlighting the growth of 34.2% in trade applications, including services. Industrial sector consultations grew 6.8%, highlighting the demand of the sectors of transportation equipment, food products and coke, oil and fuel.

Rural credit transactions, excluding those contracted by the BNDES, increased 6.7% in the quarter, reaching R$83.6 billion, with emphasis on the rise of 8.1% recorded in those aimed at costs, which accounted for 43.9% of the total, whilst the shares for investment and marketing reached 51.5% and 4.6%, respectively.

In relation to the housing loans portfolio, disbursements based upon savings accounts funds totaled R$23.9 billion in the first eight months of the year, up 59.5% in relation to the same period in 2009, while the total number of house units financed grew by 34.5%.

Nonearmarked credits

The balance of nonearmarked credit operations reached R$1,079 billion in October, for a 5.3% increase in the quarter and 15.7% in twelve months. The proportion of these transactions in the financial system portfolio fell from 68.2% in October 2009 to 65.6%.

Table 3.4 – Nonearmarked credit operations

R$ billion

	2010				% growth	
	Jul	Aug	Sep	Oct	3 months	12 months
Total	1 025.0	1 042.2	1 061.6	1 078.9	5.3	15.7
Corporations	514.0	521.2	532.9	541.5	5.3	14.3
Reference credit[1/]	425.1	430.6	442.0	449.6	5.8	15.3
Domestic funding	374.0	378.2	390.4	397.4	6.2	20.5
External funding	51.0	52.3	51.6	52.2	2.4	-12.9
Leasing[2/]	44.2	44.3	43.1	41.9	-5.1	-16.0
Rural[2/]	2.9	3.2	3.3	3.1	6.6	-21.6
Others[2/]	41.8	43.1	44.4	46.8	11.9	56.7
Individuals	511.0	521.1	528.7	537.4	5.2	17.1
Reference credit[1/]	376.6	384.2	393.7	402.7	6.9	26.6
Credit unions	23.0	23.4	23.8	24.4	5.9	18.7
Leasing	53.5	51.9	50.5	49.3	-7.9	-23.2
Others	57.9	61.4	60.8	61.1	5.5	9.0

1/ Interest rate reference credit, defined according to Circular n. 2,957 dated 12.30.1999.
2/ Operations backed by domestic resources.

Transactions carried out in the segment of individuals, which closed at R$537.4 billion, increased 5.2% in the quarter and 17.1% in twelve months. In the framework of reduced interest rates and lengthened average terms, it should be highlighted the respective expansions of 10.7% and 44.4% recorded in the segment of vehicle financing. Payroll-deducted loans, accounting for 60.4% of personal credit portfolio, grew 6.3% in the quarter and 28.7% in twelve months.

The balance of corporate transactions reached R$541.5 billion in October, rising 5.3% in the quarter and 14.3% in twelve months, with emphasis on the respective expansions of 6.4% and 23.6% recorded by working capital. Loans backed by external funds, reflecting the performance of contracting under Advance on Exchange Contracts (ACC) varied 2.4% in the quarter and -12.9% in twelve months.

Figure 3.3 – Interest rates on nonearmarked credit

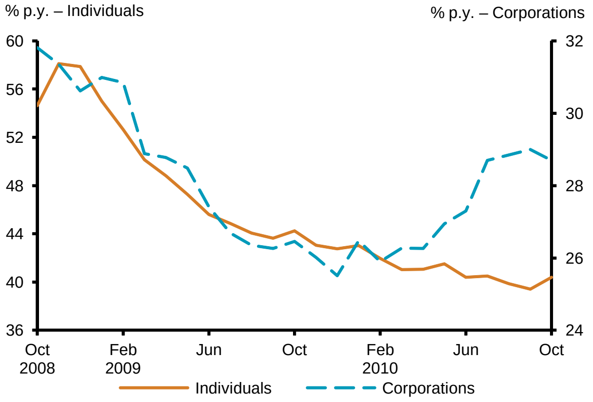


Figure 3.4 – Average spread on nonearmarked credit

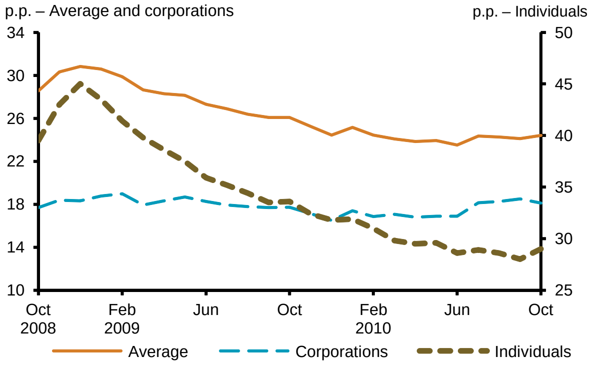
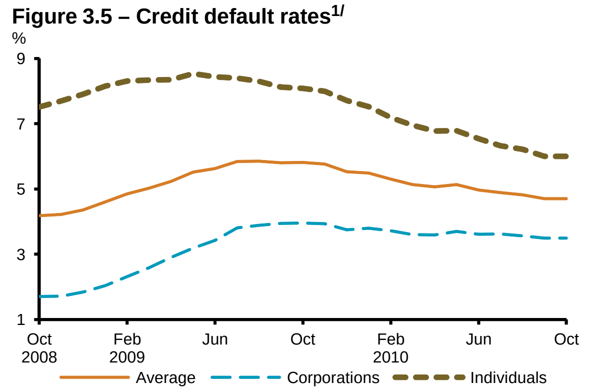
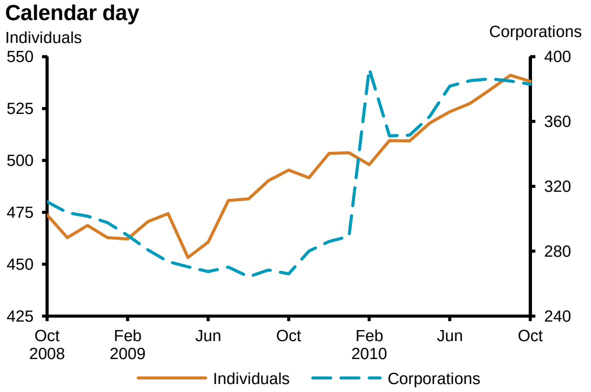


Figure 3.5 – Credit default rates1/



1/ Nonearmarked credit in arrears of more than 90 days.

Figure 3.6 – Average term for credit operations – Calendar day



Interest rates and default

The average interest rate for reference credit operations reached 35.4% p.a. in October, registering stability in the quarter and a drop of 0.2 p.p. compared to the same month of 2009. The banking spread totaled 24.4 p.p. in October, for respective changes of 0.1 p.p. in the quarter and -1.6 p.p. in twelve months.

The average cost of transactions carried out in the individual segment reached 40.4% in October, dropping 0.1 p.p. in the quarter and 3.8% in twelve months, emphasizing the annual falloffs in the rates for personal loans and purchase of vehicles. The average rate for transactions contracted in the corporate segment closed at 28.7%, registering stability in the quarter and increasing by 2.2% in twelve months.

The default rate of reference credit modalities, which have followed a downward trend since mid 2009, reached 4.7% in October. The quarterly fall of 0.2 p.p. resulted from respective decreases of 0.3 p.p. and 0.1 p.p. in the segments of individuals and corporations.

The average term of the reference credit portfolio reached 456 days in October, rising 4 days in the quarter and 87 days in twelve months. In the quarter under analysis, the average term of household loans increased by 11 days in s, influenced by the segment of vehicle purchase, and decreased by 2 days in the corporate segment.

3.2 Monetary aggregates

The average daily balance of the restricted money supply (M1) totaled R$250.9 billion in October, expanding by 5.2% in the quarter and 18.8% in twelve months. The monetary base totaled R$176.9 billion, rising 6.4% and 21.6% in the same comparison bases.

Considering the end-period balances, the monetary base stood at R$177.4 billion in October. The quarterly growth of R$14.9 billion reflected, in particular, the impact of R$38.8 billion in net Central Bank currency purchases on the interbank foreign exchange market, partly offset by the impact of the National Treasury transactions, R$7.3 billion, and compulsory reserve requirements, R$6.8 billion.

The money supply, in the M2 concept, increased 5.4% in the quarter and 13.3% in twelve months, totaling R$1.3 trillion. The M3 reached R$2.5 trillion, rising 6.2% and 15.6%,

Figure 3.7 – Monetary base and M1 – Average daily balances

R$ billion

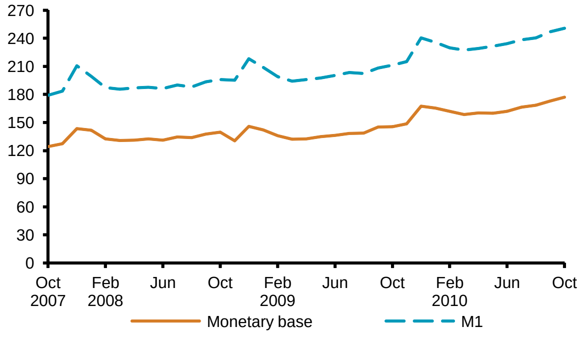


Figure 3.8 – Broad money supply

12-month % growth

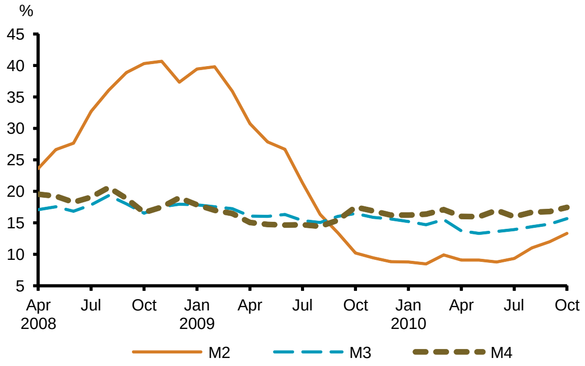
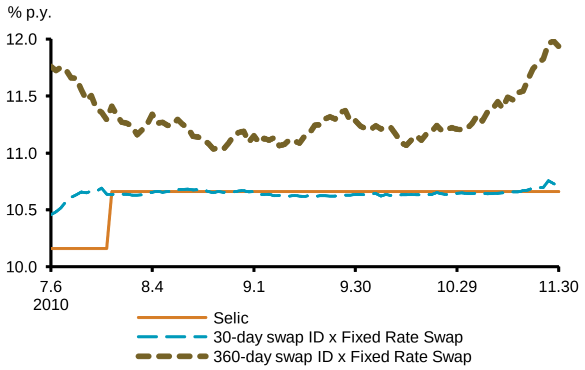
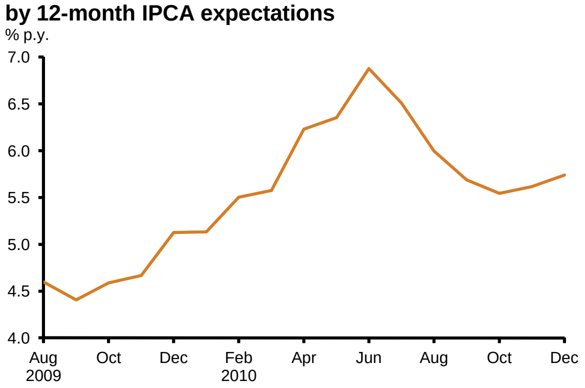


Figure 3.9 – Interest rate



Source: BM&F

Figure 3.10 – Ex-ante real interest rate – Deflated by 12-month IPCA expectations



respectively, while the M4 aggregate totaled R$3 trillion, growing by 6.5% and 17.5%.

With the goal of maintaining the process of gradual withdrawal of incentives introduced in response to the worsening of the international financial crisis and seeking to ease liquidity conditions in the prospective scenario, the Central Bank issued, on December 3, 2010, the Circular no. 3,513, which raised the percentage of reserve requirements on fixed-term deposits from 15% to 20%. Deduction limits were raised as follows: from R$2 billion to R$3 billion for financial institutions with reference assets lower than R$2 billion: and from R$1.5 billion to R$2.5 billion for those with reference assets exceeding R$2 billion and lower than R$5billion. The maximum deduction limit for amounts related to the acquisition of securities and interbank deposits was reduced from 45% to 36%. Issues of Financing Bills remained exempt from reserve requirements.

Issued on the same date, the Circular no. 3,514 increased the rate of additional liability on demand and fixed-term deposits from 8% to 12%. The deduction limits increased from R$2 billion to R$2.5 billion for institutions with reference assets lower than R$2 billion and R$1.5 billion to R$2 billion for those with assets between R$2 billion and R$5 billion. These measures became effective as of the calculation period beginning December 6, 2010 with an estimated monetary impact of R$61 billion.

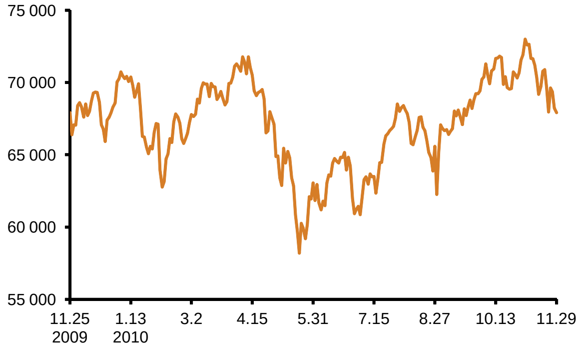
Additionally, the CMN, through Resolution no. 3,931, dated December 3, 2010, raised the maximum guarantee value of deposits and loans secured by the Credit Guarantee Fund (FGC), from R$60,000 to R$70,000, and defined the gradual reduction of the limit for raising Fixed-term Deposits with Special FGC Guarantee (DPGE) at a rate of 20 p.p. per year, beginning on January 1, 2012, up to 2016.

Real interest rates and market expectations

The curve of future interest rates for ID X pre swap contracts, demonstrating expectations for the trend of the basic interest rate and rises in risk premiums, showed, in late November, an increase in slope for all vertices. The 360-day ID x pre swap contracts rose by 84 b.p. in the quarter, to 11.94% p.a.

The real *ex-ante* Selic rate for the next twelve months, calculated by the Market Report survey dated December, 10, reached 5.7% p.a., compared to 6% p.a. in August. This reduction reflected, in particular, the rise, from 4.9% to 5.2%, of 12-month IPCA expectations.

Figure 3.11 – Ibovespa
Points



Source: Bovespa

Figure 3.12 – Stock exchanges
Sep 2009 = 100

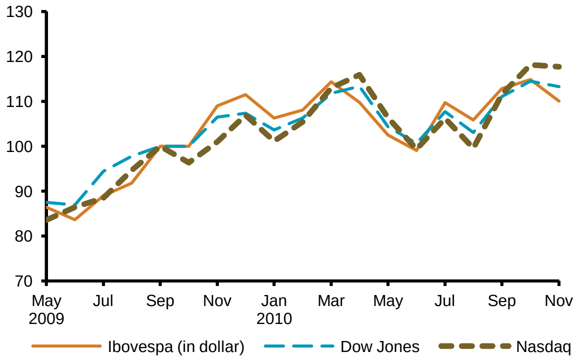
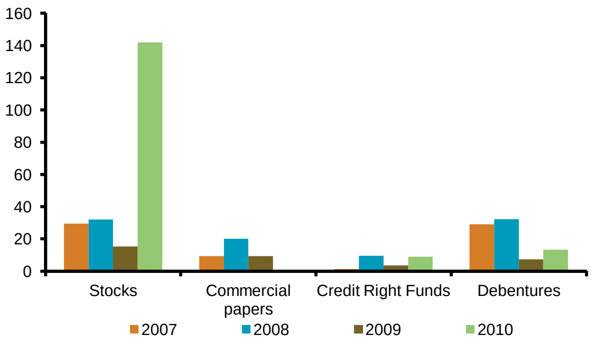


Figure 3.13 – Primary issues in the capital market
R$ billion – Accumulated through November



Source: CVM

Table 3.5 – Public sector borrowing requirements – Primary result

Segment	2008		2009		Oct 2010[1/]	
	R$ billion	% GDP	R$ billion	% GDP	R$ billion	% GDP
Central Government	-71.3	-2.4	-42.4	-1.4	-74.2	-2.1
Sub-national governments	-30.6	-1.0	-21.0	-0.7	-22.2	-0.6
State companies	-1.7	-0.1	-1.3	-0.0	-2.7	-0.1
Total	-103.6	-3.4	-64.8	-2.1	-99.1	-2.8

1/ Twelve-month accumulated data up to october.

Capital markets

The São Paulo Stock Exchange Index (Ibovespa), following an upward trend up to mid-November, when it again exceeded the threshold of 70,000 points, started to show accentuated volatility, closing the quarter at 67,705 points. The market value of the index listed companies grew 11% in the quarter, reaching R$2.5 trillion at the end of November, while the average daily trading volume increased by 24.8%.

Measured in dollars, Ibovespa rose 6.3% in the quarter. In the same period, the Dow Jones and Nasdaq indices rose 9.9% and 18.9%, respectively.

Business financing in the capital market through issues of shares, debentures, promissory notes and placement of receivables-backed, totaled R$164.4 billion in the first eleven months of 2010, compared to R$36.5 billion in the same period of 2009, with emphasis on the primary issues of R$120.2 billion of Petrobras shares, a record volume in the Brazilian stock exchange.

3.3 Fiscal Policy

In November, the government submitted to the National Congress a bill proposing the exclusion of the results of the Eletrobras Group companies from the public sector primary surplus and, hence, the amendment of the goals stated in the Budget Guidelines Law (LDO) for 2010, of 3.3% of GDP to 3.1% of GDP, and for 2011, of R$125.5 billion to R$117.9 billion.

Fiscal statistics released by the Central Bank began to exclude the Eletrobras group companies, as prescribed by Decree no. 7,368, dated November 26, 2010, which deals with the Federal Government budget and financial programming.

Public sector borrowing requirements

The consolidated public sector primary surplus totaled R$86.7 billion, 2.99% of GDP, in the first ten months of the year, rising 0.95 p.p. of GDP compared to the same period in 2009. This performance reflected the impact of increased surpluses registered by the Central Government and state enterprises, and the fall of those relating to regional

Figure 3.14 – National Treasury gross revenue
Jan-Oct

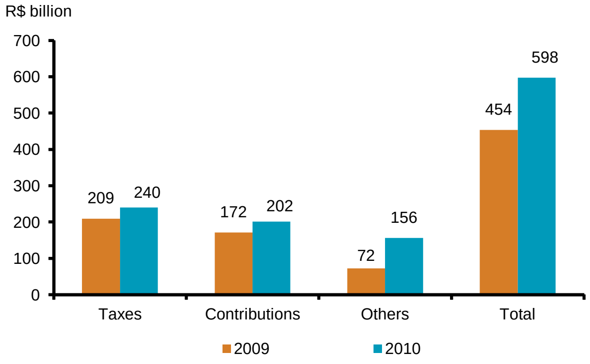


Table 3.6 – National Treasury expenditures
Jan-Oct

	2009		2010	
	R$ million	% GDP	R$ million	% GDP
Total	273 623	10.7	368 142	12.7
Personnel and payroll charges	121 383	4.7	132 788	4.6
Capital and current expenditures	151 306	5.9	234 357	8.1
Workers Support Fund	23 180	0.9	25 185	0.9
Subsidies and economic	3 898	0.9	7 586	0.9
subventions	3 898	0.2	7 586	0.3
Loas/RMV	15 671	0.6	18 431	0.6
Investment	23 940	0.9	36 104	1.2
Other capital expenditures	84 617	3.3	147 050	5.1
National Treasury transfers				
to the Central Bank	934	0.0	997	0.0

Source: Minifaz/STN

Table 3.7 – Social security primary result
Jan-Oct

R$ billion

	2009	2010	Var. %
Gross inflow	155.6	181.9	16.9
Cash refunds	-0.4	-0.5	14.4
Transfers to third parties	-15.5	-17.9	15.2
Net inflow	139.6	163.5	17.1
Social Security benefits	181.1	205.5	13.4
Primary result	-41.5	-41.9	1.0
Net inflow/GDP	5.4%	5.6%	
Social Security benefits/GDP	7.1%	7.1%	
Primary result/GDP	-1.6%	-1.4%	

governments. The accumulated surplus in twelve months reached 2.85% of GDP.

Federal Government gross revenues totaled R$597.8 billion in the first ten months of 2010, rising 31.8% compared to the same period in the previous year. This expansion, equivalent to 2.9 p.p. of GDP, reflected the favorable impact of the economic performance on income tax, as the levy of R$74.8 billion on the onerous assignment of petroleum exploration registered in September. Excluding the mentioned sale, the Federal Government revenues increased by 15.3%, equivalent to 0.3 p.p. of GDP in the period.

National Treasury expenditures totaled R$368.1 billion in the first ten months of 2010, increasing 34.5% compared to the same period in the previous year. It should be noted that this growth, accounting for 2 p.p. of GDP, reflected in particular the capitalization of Petrobras in September (R$42.9 billion). Excluding this contribution, the increase in Treasury expenditures reached 16.7% in the period, 0.5 p.p. of GDP. Spending on personnel and taxes grew 9.4%, and that relating to costs and capital expenditures, excluding capitalization, 26.5%, with emphasis on the 51% expansion in investments. Expenditures related to the Growth Incentive Program (PAC), which can be deducted from the primary surplus, amounted to 0.69% of GDP in the 12-month period ended in October.

The Social Security deficit reached R$41.9 billion in the first ten months of the year, falling 0.17 p.p. of GDP compared to the same period in 2009. Net income tax, reflecting the growth in wages, increased 17.1%, whilst expenditure on social security benefits, reflecting respective increases of 8.8% and 3.1% in the average value of pensions and welfare as well as the average monthly amount of benefits paid, increased by 13.4%.

The total Central Government – National Treasury, Social Security and Central Bank – revenues rose 28.2% on the same comparison basis, while spending grew by 26.1%. Excluding onerous assignment transactions of subsalt and the capitalization of Petrobras, which are atypical transactions, without correspondence in the previous year, central government revenues grew less than expenditures, for respective changes of 15.5% and 16.6%.

Transfers to regional governments totaled R$111.3 billion in the first ten months of the year, rising 9.6% compared to the same period in the previous year. This trajectory reflected the expansion of resources transferred through equity funds, in response to the favorable performance of shared taxes; transfers related to the exploration of oil and natural gas, influenced by rising international market prices; and transfers related to the Contribution on Intervention in the Economic Domain (Cide), resulting from the rise in rates effective as of June 2009.

The primary surplus of states and municipalities, and state enterprises experienced respective variations of -0.05 p.p. of GDP and 0.04 p.p. of GDP compared to that recorded in the first ten months of 2009.

Income relating to the Tax on the Circulation of Merchandise and Services (ICMS), the most dynamic regional tax, and Vehicle Excise Duty (IVPA) registered respective increases of 19.6% and 3.8% in the first nine months the year, compared to the same period in 2009.

Nominal appropriated interests totaled R$157.3 billion in the first ten months of the year. The nominal public sector deficit, which includes the primary result and the nominal appropriated rates, reached R$70.6 billion, equivalent to 2.44% of GDP, registering a reduction of 1.04 p.p. of GDP compared to the same period of 2009. The financing of this deficit occurred through expansion of net banking debt, debt securities and other domestic funding sources, including the monetary base, partly offset by the drop in net foreign financing.

Central Bank open market operations

National Treasury primary transactions with federal public securities led to a monetary contraction of R$7.2 billion in the quarter ended October, as a result of placements of R$129.4 billion and redemptions of R$122.2 billion. Exchange transactions totaled R$8.9 billion, of which 73.5% referring to National Treasury Notes – Series B (NTN-B). Anticipated redemptions totaled R$4.9 billion, of which 99.3% referring to NTN-B.

The average daily balance of Central Bank financing and go-around transactions totaled R$413.4 billion in October. The quarterly growth of 1.9% reflected the impact of rises registered in six month transactions, from R$94.2 billion in July to R$126.3 billion in October; for those with terms lower than two weeks, from of R$67.6 billion to R$70.2 billion; and the reduction, from R$243.8 billion to R$216.8 billion, of those with terms from two weeks to three months.

Table 3.8 – Public sector borrowing requirements
Jan-Oct

	2008		2009		2010	
	R$ billion	% GDP	R$ billion	% GDP	R$ billion	% GDP
Uses	11.7	0.5	89.0	3.5	70.6	2.4
Primary	-125.5	-5.0	-52.3	-2.0	-86.7	-3.0
Interest	137.2	5.5	141.4	5.5	157.3	5.4
Sources	11.7	0.5	89.0	3.5	70.6	2.4
Domestic financing	51.7	2.1	132.3	5.2	147.4	5.1
Securities financin	132.4	5.3	276.2	10.8	116.6	4.0
Bank financing	-68.7	-2.8	-144.7	-5.6	17.6	0.6
Others	-12.0	-0.5	0.9	0.0	13.1	0.5
External financing	-40.0	-1.6	-43.3	-1.7	-76.8	-2.6

Figure 3.19 – Net financing position of the federal public securities – Daily average

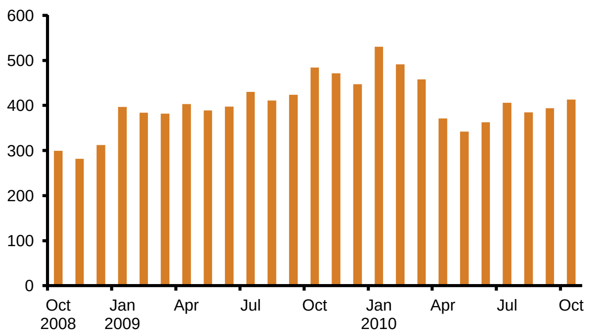


Figure 3.20 – Central Bank repo operations – Maturity – Aveage daily balances

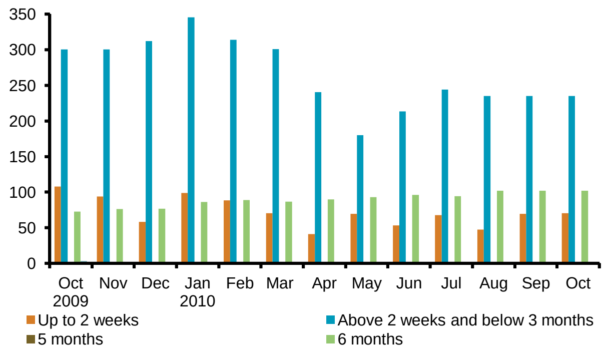
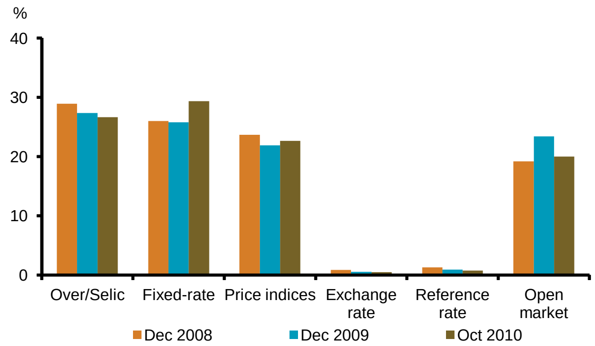


Figure 3.21 – Federal securities debt structure by indexing factor[1/]



1/ It does not include swap.

Federal securities debt

The federal debt measured by the portfolio position totaled R$1,552.7 billion in October, 44.6% of GDP, registering variations of 0.2 p.p. of GDP compared to July and -0.1 p.p. of GDP in twelve months. The quarterly increase reflected the impact of net primary market issues, R$2.9 billion, and the incorporation of nominal interests, R$41 billion, partly offset by the effect of the exchange rate appreciation registered in the quarter, 3.2%.

Of the total federal debt, the participation of securities indexed to the over/Selic rate and to price indices posted quarterly decreases of 0.8 p.p. and 1.3 p.p. in October, contrasting with expansions in fixed-rate securities, 2.01 p.p., and Central Bank financing through open market transactions, 0.1 p.p.

The repayment schedule of debt securities on the market, with the exception of financing transactions, registered the following maturity schedule in October: 1.1% of the total maturing in 2010; 21.5% in 2011; and 77.4% as of January 2012. Securities maturing in 12 months accounted for 20.2% of the total securities debt on the market, slightly lower than the percentage range of 24% to 28% established by the PAF in 2010. The average debt maturity reached 41.2 months.

Public sector net debt

The public sector net debt (PSND) totaled R$1,436.3 billion in October, 41.3% of GDP, falling 2.1 p.p. of GDP compared to December 2009. This decline reflected the contributions of the primary surplus, 2.5 p.p. of GDP, current GDP growth, 4.2 p.p., and the privatizations and acknowledgement of debts, both 0.1 p.p., partly offset by expansions associated with the appropriation of nominal interest rates, 4.5 p.p. of GDP, and the impact of currency exchange appreciation, 0.3 p.p. of GDP.

The PSND registered, in particular, growth in creditor installments linked to Long Term Interest Rates (TJLP) – due to the increase of Federal Government assets with the BNDES through issue of federal securities – and the Selic rate.

The Gross General Government Debt, which comprises the Federal Government, INSS, state governments and municipal governments – reached R$2,087.8 billion, 60% of GDP, in October, falling 2.8 p.p. of GDP compared to December 2009.

Figure 3.22 – Profile of maturities of the securities debt

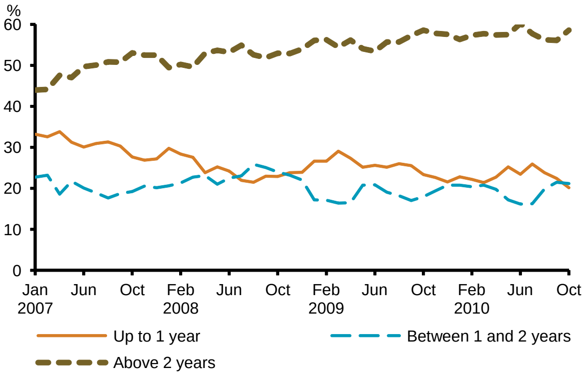


Figure 3.23 – NPSD – Percentage share of indexator

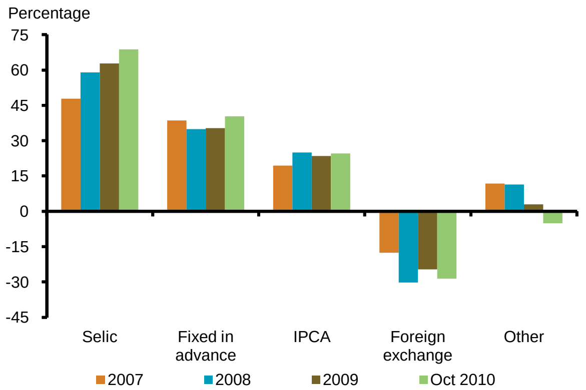


Table 3.9 – Net debt growth

Conditioning factors

	2008		2009		Oct 2010	
	R$ million	% GDP	R$ million	% GDP	R$ million	% GDP
Total net debt – Balance	1168 238	38.9	1362 711	43.4	1436 288	41.3
Flows	**Accumulated in the year**					
Net debt – Growth	-43 524	-6.7	194 472	4.5	73 577	-2.1
Conditioning factors	-43 524	-1.4	194 472	6.2	73 577	2.1
PSBR	61 927	2.1	106 242	3.4	70 632	2.0
Primary	-103 584	-3.4	-64 769	-2.1	-86 677	-2.5
Interest	165 511	5.5	171 011	5.4	157 309	4.5
Exchange adjustment	-78 426	-2.6	80 886	2.6	9 367	0.3
Domestic securities	3 180	0.1	-3 414	-0.1	809	0.0
debt[1/]	-81 606	-2.7	84 300	2.7	8 557	0.2
External debt	-26 394	-0.9	10 907	0.3	-1 591	0.0
Others[2/]	0	0.0	0	0.0	0	0.0
Skeletons	135	0.0	- 345	0.0	-2 088	-0.1
Privatizations	- 767	0.0	-3 217	-0.1	-2 742	-0.1
GDP growth effect		-5.2		-1.7		-4.2

1/ Domestic dollar – Indexed securities.
2/ Parity of the basket of currencies in the net external debt.

3.4 Conclusion

Economic activity is still being sustained by high domestic demand growth rates. Accordingly, the credit market continues to give a significant contribution in the financing of investment and aggregate consumption. Earmarked operations have been boosted by the significant role played by the BNDES in providing funds for infrastructure projects and the purchase of machinery and equipment for small and medium enterprises, in addition to the acceleration of housing credit growth. Meanwhile, nonearmarked credit loans continue to show a robust performance in the area of household transactions, with emphasis on payroll-deducted and auto loans.

The credit market has been also benefited from declining interest rates for loans to individuals, which reached historic lows. The stability of default rates at low levels also contributed to the scenario of credit expansion.

Although the pace of economic activity has decelerated in recent months, retail sales continued to show strong dynamism, a development associated with both the performance of the labor market and of the credit market, the latter stimulated by positive expectations and favorable supply conditions. In this scenario, the CMN and the Central Bank adopted macro-prudential measures aimed at adjusting the financial system liquidity levels through the rise in reserve requirements and the discouragement of transactions potentially harmful to financial institution's household balance sheets or the balance between contracted volumes and guarantee values. These measures improved credit market regulatory instruments with the goal to ensure its stability and prevent the emergence of risks that could jeopardize the economic activity.

The expansion of the public sector primary surplus in the first ten months of the year was due to a significant revenue growth as compared to expenditures, highlighting the reversal of this relationship when excluding the impact of atypical transactions with no parallel in the previous year, such as the onerous assignment of subsalt and the capitalization of Petrobras. The PSND/GDP ratio remains on a downward trajectory, emphasizing this trend is reinforced by the fiscal policy objectives defined in the budget law.

Capital Structure of Public Companies in Brazil

The aim of this Box is to examine the financial structure of public companies in Brazil during the 2005-2009 periods, with emphasis on the development of debt and the trend of the composition of ordinary sources of funding.

It is based on a sample of publicly traded companies with shares traded at BM&FBOVESPA S.A. – Securities, Commodities and Futures Exchange (BM&FBOVESPA), over the five-year period ending 2009[1]. The filters used for the construction of the sample mentioned prioritized non-financial companies that reported net operating revenues exceeding R$30 million in the 2009 fiscal year, a total of 147[2] that jointly registered sales of R$287.4 billion in December 2009. These companies are spread across 20 segments of the economic sector classification as suggested by Economática.

Capital structure by maturity, seen in Table 1, shows that short-term liabilities (up to one year), represented by current liabilities of the sample companies, reported relative stability in the five-year period, accounting, on average, for 19.6% of the total of funds in the period. Long-term bonds (over one year), represented by non-current liabilities, comprised, on average, 29.6% of the total, registering a significant increase in the last two years.

Table 1 – Equity structure by maturity

% share

	2005	2006	2007	2008	2009	Average
Third party captital	48.4	47.4	45.9	52.7	51.6	49.2
Current liabilities	19.4	19.7	19.0	20.5	19.4	19.6
Non-current liabilities	29.0	27.7	26.9	32.2	32.2	29.6
Shareholder's equity	51.6	52.6	54.1	47.3	48.4	50.8
Total	100.0	100.0	100.0	100.0	100.0	100.0

Debt accounted, on average, for 49.2% of funds raised over the five-year period, while the proportion of shareholder capital, after experiencing a sharp annual fall of 6.8 p.p. in 2008, reached 50.8%. It

1/ Considering that the data analyzed is extracted from the financial statements of companies registered in the Economática system, the analysis will focus on the situation as of December 31 of each year, with 2009 being the latest fiscal year available.

2/ Not including Petrobras and Vale do Rio Doce, which have too great a size discrepancy in relation to other companies.

Table 2 – Equity structure

% annual growth

	2006	2007	2008	2009
Third party captital	6.0	6.9	36.1	11.3
Current liabilities	10.0	6.5	27.9	8.0
Non-current liabilities	3.3	7.2	41.9	13.4
Shareholder's equity	10.2	13.7	3.8	16.6
Total resources	8.1	10.5	18.5	13.8

Table 3 – Financial and non-financial liabilities to third parties

% share

	2005	2006	2007	2008	2009	Average
Financial	47.4	48.3	46.9	53.1	49.6	49.1
Non-financial	52.6	51.7	53.1	46.9	50.4	50.9
Total	100.0	100.0	100.0	100.0	100.0	100.0

Table 4 – Financial debt by modalities and terms

% share

	2005	2006	2007	2008	2009	Average
Short-term debt	23.1	24.1	20.4	22.6	23.5	22.7
Financing	20.1	19.3	19.1	20.7	21.2	20.0
Debentures	3.0	4.8	1.3	1.9	2.3	2.7
Long-term debt	76.9	75.9	79.6	77.4	76.5	77.3
Financing	62.5	59.5	61.4	63.8	63.7	62.2
Debentures	14.4	16.4	18.2	13.6	12.8	15.1
Total	100.0	100.0	100.0	100.0	100.0	100.0

Table 5 – Partiicipation of supplier's credit

%

	2005	2006	2007	2008	2009	Average
Suppliers/current liabilities	24.8	26.7	26.8	26.2	23.7	25.6
Suppliers/total resources	4.8	5.3	5.1	5.4	4.6	5.0

is worth emphasizing that this decline reflected, in particular, the impact of the intensifying global crisis in the second half of 2008 on the aggregate net profit of the companies considered, which fell 12% in that year. The resumption of activity in 2009 supported a reversal of this movement, expressed in a 29% annual rise in net profit. The annual trends of debt capital and aggregated shareholder capital are shown in Table 2, highlighting the contrast between the annual growth rates seen in 2008 in debt capital, 36.1%, and in shareholder capital, 3.8%.

Debt capital is composed of non-financial debt, such as supplier credit, various operational credits for payments (salaries, social charges, taxes, services, etc.), and typical financial debts such as loans, financing and debentures. This breakdown, as seen in Table 3, shows the relative stability of the proportions of the two modes in the debt capital total, only registering statistical change in 2008, also associated with the impact of the global crisis.

Table 4 records the breakdown of financial debt by financing and debentures, segmented by length of maturity. On average, short and long-term financing accounted for 82.2% of debt in the period. Regarding debentures – the predominant fundraising instrument within large companies – it is worth mentioning the proportion of long-term transactions.

In parallel, it is worth highlighting the 25.6% average proportion of supplier’s credit – a mechanism with no explicit cost – in current liabilities and 5% in the total of resources used for financing, both of which registering relative stability in the recording period (Table 5).

In summary, equity accounted for an average of 50.8% of the funds used for business financing that form the sample over the five-year period ending in 2009, and debt capital make up 49.2%. Specifically with respect to the last segment, the proportion of long-term (non current) and short-term liabilities (current) reached, on average, 60.2% and 39.8% in the period, suggesting a comfortable capital structure with relatively low risk.

The breakdown of debt capital shows that financing debts comprised, on average, 49.1% of these liabilities, over five years. Additionally, it is worth emphasizing the stability of its share during the period and its concentration in loans and long-term financing.

The worsening of the global financial crisis has created short-lived effects, mostly in 2008, on the capital structure of companies, with emphasis on increased indebtedness, reflecting the expansion of debt and/or the decline in net profits. Additionally, it is important to emphasize that the low risk of financial leverage of the publicly traded companies is an indication that there would be enough room for funding, in relation to new investment opportunities, within a framework of sustainable expansion in the Brazilian economy. The challenge is to ensure a consistent supply of appropriate financing, both in terms of cost and maturity.

Credit transactions in the Automotive Sector and Connected Activities

Credit transactions targeted to the purchase of automotive vehicles have grown significantly in recent years, contributing to sustain the activity level in the automotive industry and in the economy as a whole. With the aim of contributing to the analysis of the sector's economic performance, this Box evaluates the trajectory of credit transactions for the acquisition of vehicles, the production and marketing of cars, trucks, buses, motorcycles and agricultural machinery as well as auto parts, components and accessories.

Favorable credit market conditions, expressed by reduced interest rates and lengthened maturities, in addition to macroeconomic stability and positive trajectory of employment and income indicators led to the expansion of financing and commercial leasing operations for vehicles and agricultural machinery.

Thu, the stock of the sector's credit operations, taken into account both transactions with individuals and corporations, as shown in Table 1, totaled R$217 billion in September 2010, increasing by 232.1% in comparison to the same period in 2005. Credits targeted to individuals, encompassing direct consumer loans (CDC) and leasing operations, totaled R$176 billion, up 230.2% in the period. Meanwhile, corporate credit operations expanded 240.5%, to R$41 billion, of which R$25.2 billion involving nonearmarked resources and R$15.8 billion involving earmarked resources. It should be noted that earmarked credit operations, reflecting the relevant contribution of the Special Industrial Financing Agency (Finame) administered by the National Bank of Economic and Social Development (BNDES), grew 368.7% in the period.

Over the last five years, the supply of credit with lengthened terms and decreasing costs boosted the demand for motor vehicles and, therefore, contributed to the expansion of the segment's level of production and sales. The total output of the automotive sector – including cars, light commercial vehicles, trucks, buses and motorcycles – reached 4.6 million units in the first ten months of 2010, up 47.3% in comparison to 2005. Parallel to this, domestic sales reached 3.9 million units, compared to 2.3 million units from January to October 2005.

Financing for the production of vehicles, parts and accessories (FV) totaled R$17.6 billion in September 2010, rising 22.3% in the period, as seen in Table 1. It should be noted that the proportion of credit allocated to the automotive industry in total FV fell from 68.1% in September 2005 to 42.4%. In this segment, 70% of loans were channeled to the production of cars, 24.7% to buses, trucks and tractors and 5.3% to motorcycles. In September 2010, loans for the production of parts, spares and accessories, which now represent 57.6% of the FV, focused on contracts related to the manufacturing of engines, chassis, bodywork and other components, corresponding to 52.7% of total credit operations in this segment.

The balance of loans for the marketing of cars and auto-parts reached R$29.9 billion in September 2010, increasing 192.4% in comparison to September 2005. Of this total, 68.6% referred to loans for the marketing of new and used cars and 31.4% for the financing of auto-parts dealers.

Table 1 – Credit to the automotive sector

R$ million

Period		Output			Trade			Acquisition				Total
		Vehicles	Parts	Total	Vehicles	Parts	Total	Corporations	Individuals			
									CDC	Leasing	Total	
2005	Sep	9 808	4 588	14 396	7 096	3 124	10 220	12 053	46 218	7 080	53 298	89 966
	Dec	9 691	4 788	14 479	7 384	3 342	10 726	12 768	50 685	8 427	59 112	97 085
2006	Dec	7 435	5 219	12 654	9 427	3 980	13 407	14 251	63 475	13 877	77 352	117 664
2007	Dec	5 762	6 234	11 996	11 834	5 248	17 082	17 909	81 481	30 136	111 617	158 604
2008	Dec	7 632	6 965	14 597	17 477	7 051	24 528	20 424	82 433	56 712	139 145	198 694
2009	Dec	6 497	7 774	14 271	18 602	8 080	26 682	28 967	94 133	63 159	157 292	227 213
2010	Sep	7 458	10 142	17 600	20 490	9 391	29 882	41 038	125 515	50 456	175 971	264 491

Table 2 – Participation of credit to the automotive sector

R$ million

Period		Total credit to the automotive sector (a)	Total SFN credit (b)	Participation of the automotive sector (a)/(b)	Participation of the credit to the automotive sector no GDP
2005	Sep	89 966	564 357	15.9	4.3
	Dec	97 085	607 023	16.0	4.5
2006	Dec	117 664	732 590	16.1	5.0
2007	Dec	158 604	935 973	16.9	6.0
2008	Dec	198 694	1 227 294	16.2	6.6
2009	Dec	227 213	1 414 344	16.1	7.2
2010	Sep	264 491	1 613 631	16.4	7.7

Taken together, the balance of credit operations for the production and marketing activities of automotive vehicles and auto parts and the purchase of automotive vehicles reached R$264.5 billion in September 2010 (Table 1), rising 16.4% in comparison to the end of 2009 and 194% in comparison to September 2005. It should be noted that financing for the acquisition of vehicles accounted for 82% of this total, while the proportion of loans for the marketing and production of vehicles and auto parts totaled 11.3% and 6.7%, respectively.

Analysis of Table 2 shows that the participation of these credit operations in the total national financial system credit operations reached 16.4%, rising 0.5 p.p. over the past five years. This expansion becomes even more relevant in view of the upward trend of the ratio between the National Financial System (SFN) credit stocks and the Gross Domestic Product (GDP). Accordingly, the share of credit operations targeted to the automotive sector in the GDP moved upward from 4.3% to 7.7% in the period.

It is plausible to suppose that this trend shall be affected by the effects of Circular no. 3,515, dated December 3, 2010, on the contracting of transactions with maturities greater than 24 months. This macroprudential measure regulates, among other credit modalities, the financing and commercial leasing of vehicles whose maturity terms may jeopardize the balance between the contracted volumes and the value of vehicles constituting the guarantees for theses operations. The increase in the required capitalization of financial institutions that carry out such transactions through greater risk-weighting factor could, in principle, restrict longer-term loans, thus encouraging contracts with shorter maturities or with greater down payments. The restriction of operations with longer maturities, although could represent an eventual disincentive for credit transactions in the automotive industry, is seen as an important mechanism for maintaining the sustainable development of the credit market in the country.