Policy Responses to Commodity Price Movements – The Brazilian Experience

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Istanbul, Turkey, April 7, 2012

BANCO CENTRAL DO BRASIL

Outline

- Brazilian Macroeconomic Framework
- Commodity Price Shocks
- Policy Responses
  - Monetary Policy
  - Fiscal Policy
  - Exchange Rate Policy
  - International Reserves
  - Macroprudential Policy
- Conclusions

Macroeconomic Policy

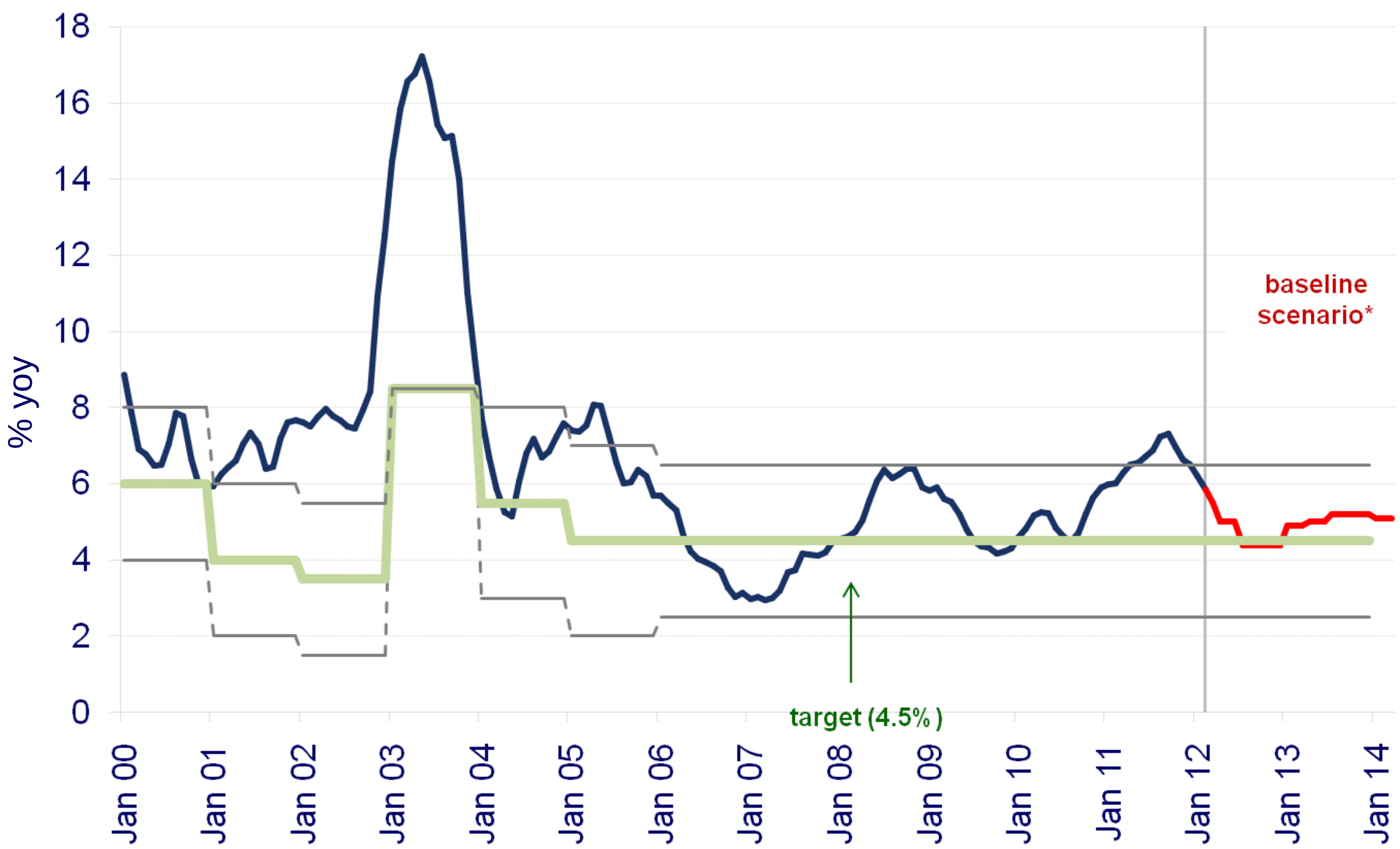
- Framework

- Inflation targeting
- Fiscal responsibility
- Exchange rate flexibility

- Complemented by

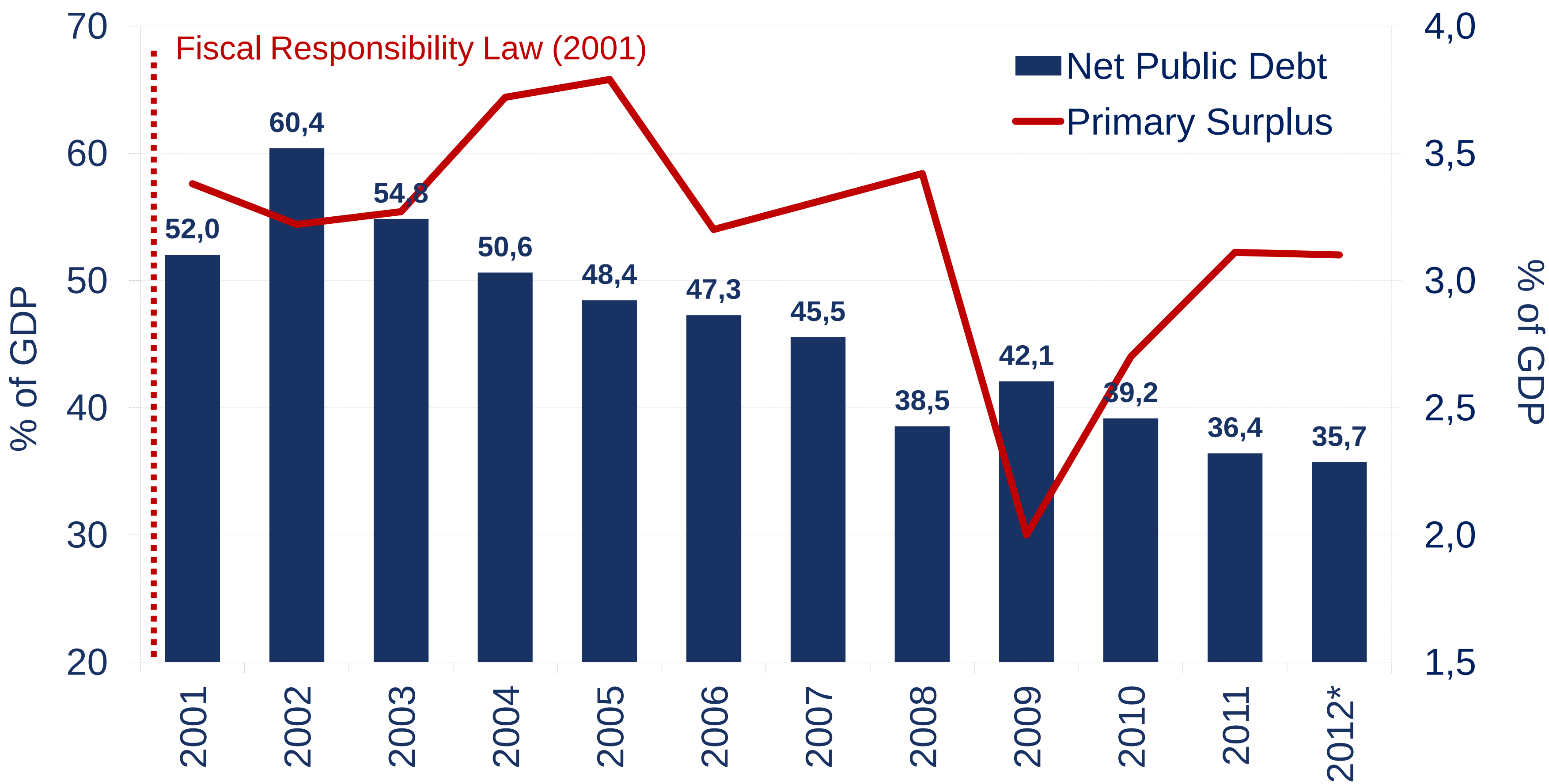
- Prudential policy and bank supervision
- International reserves

Inflation – IT Period



Sources: IBGE and BCB

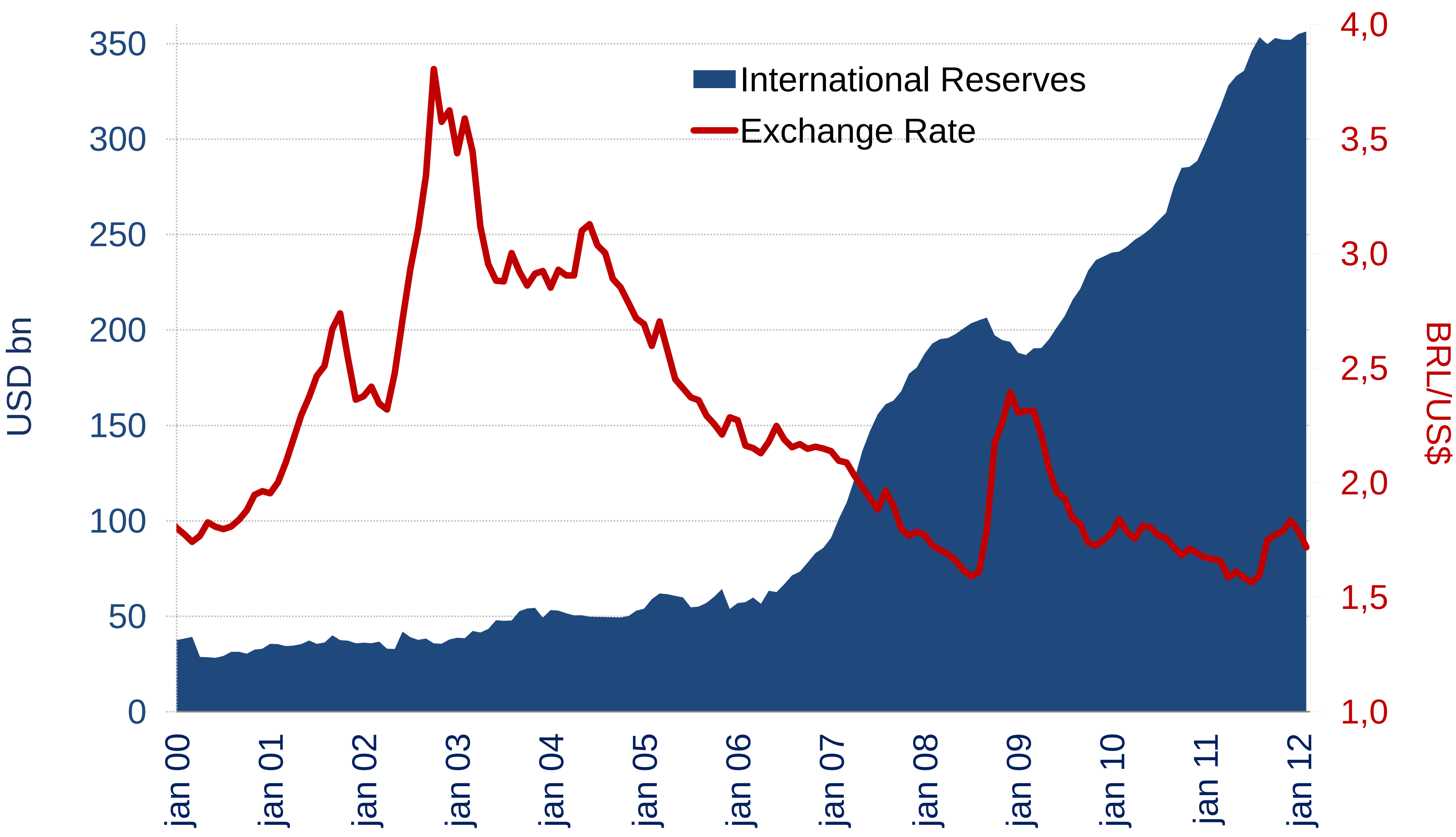
Fiscal – IT Period



*Forecast

Source: BCB

FX and International Reserves



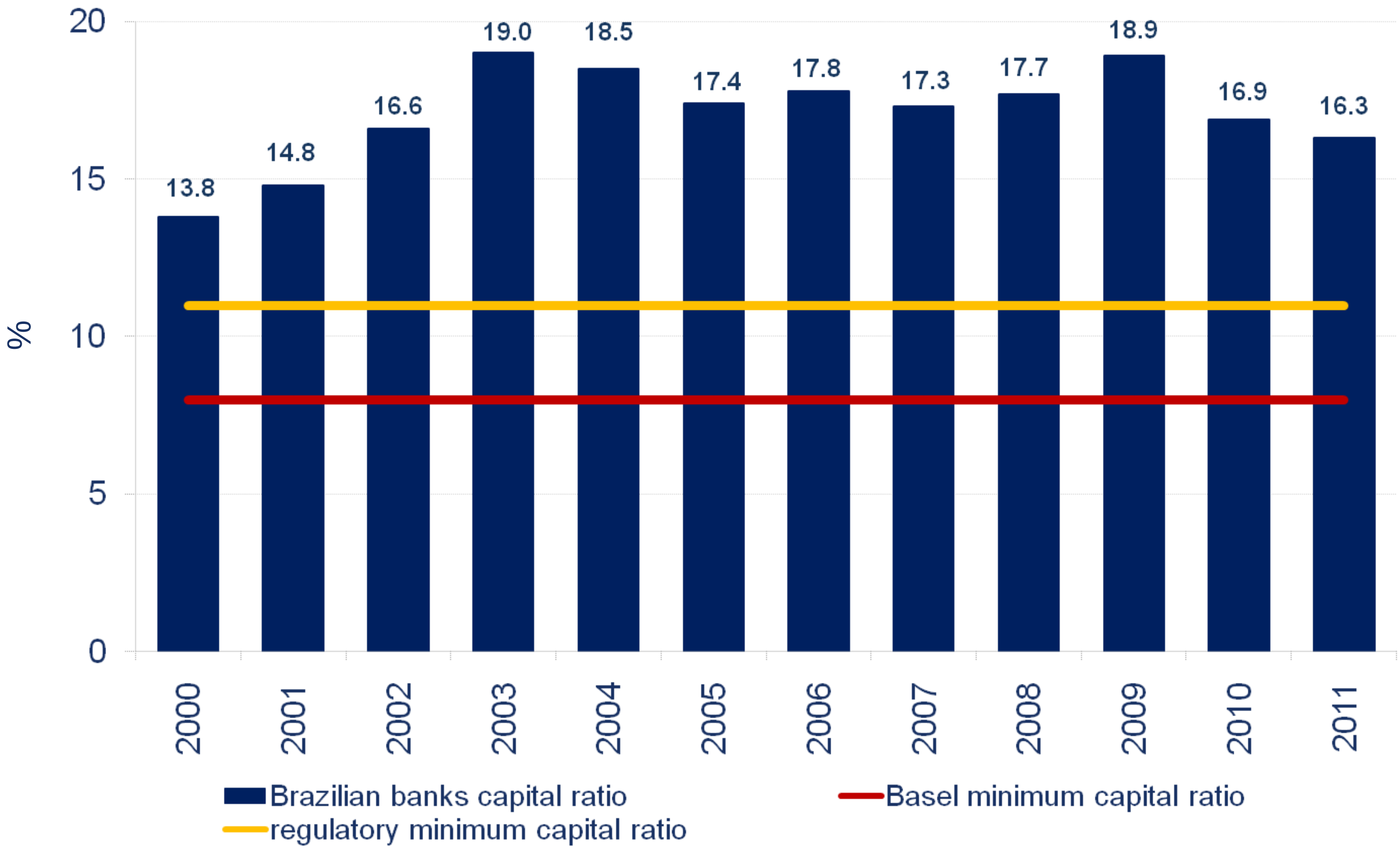
Source: BCB

Financial System - General Features

- All financial institutions are regulated and supervised
- Regulation is mostly infralegal
- Convergence to international standards (IFRS, Basel II, IOSCO)
- Brazil has been member of international forums (BCBS, G20, FSB)
- Regulation has generally been conservative

Capital Adequacy Ratio

leverage ratio: 9.9

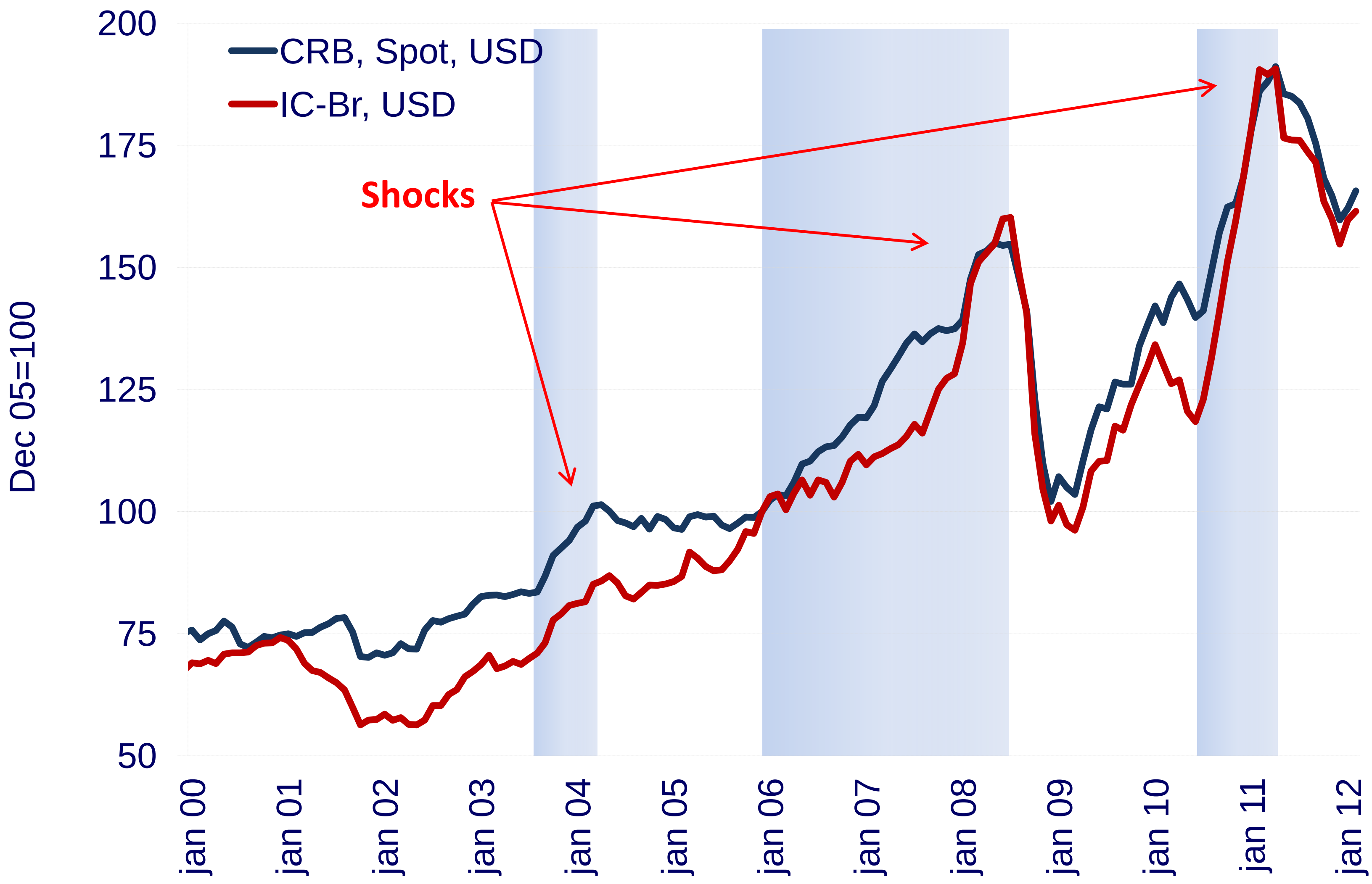


Source: BCB

Commodity Shocks

- IC-Br
- From 2000 to 2012, three commodity shocks (+20% yoy, as measured in USD)
  - Inflationary pressures
  - Improvement in terms of trade and external accounts
  - High capital inflow
  - Fast credit expansion

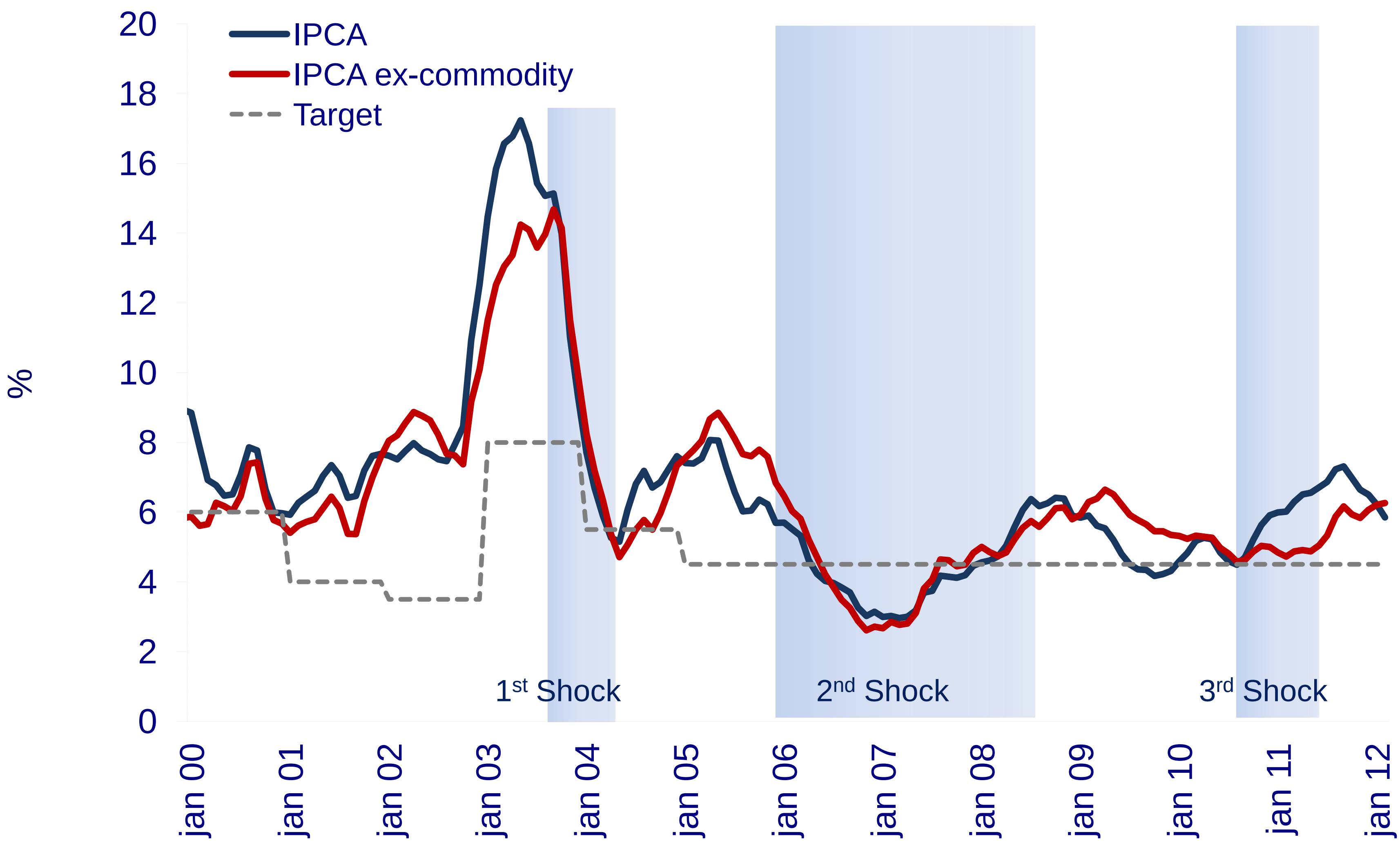
Commodity Shocks



Sources: Thomson Datastream and BCB

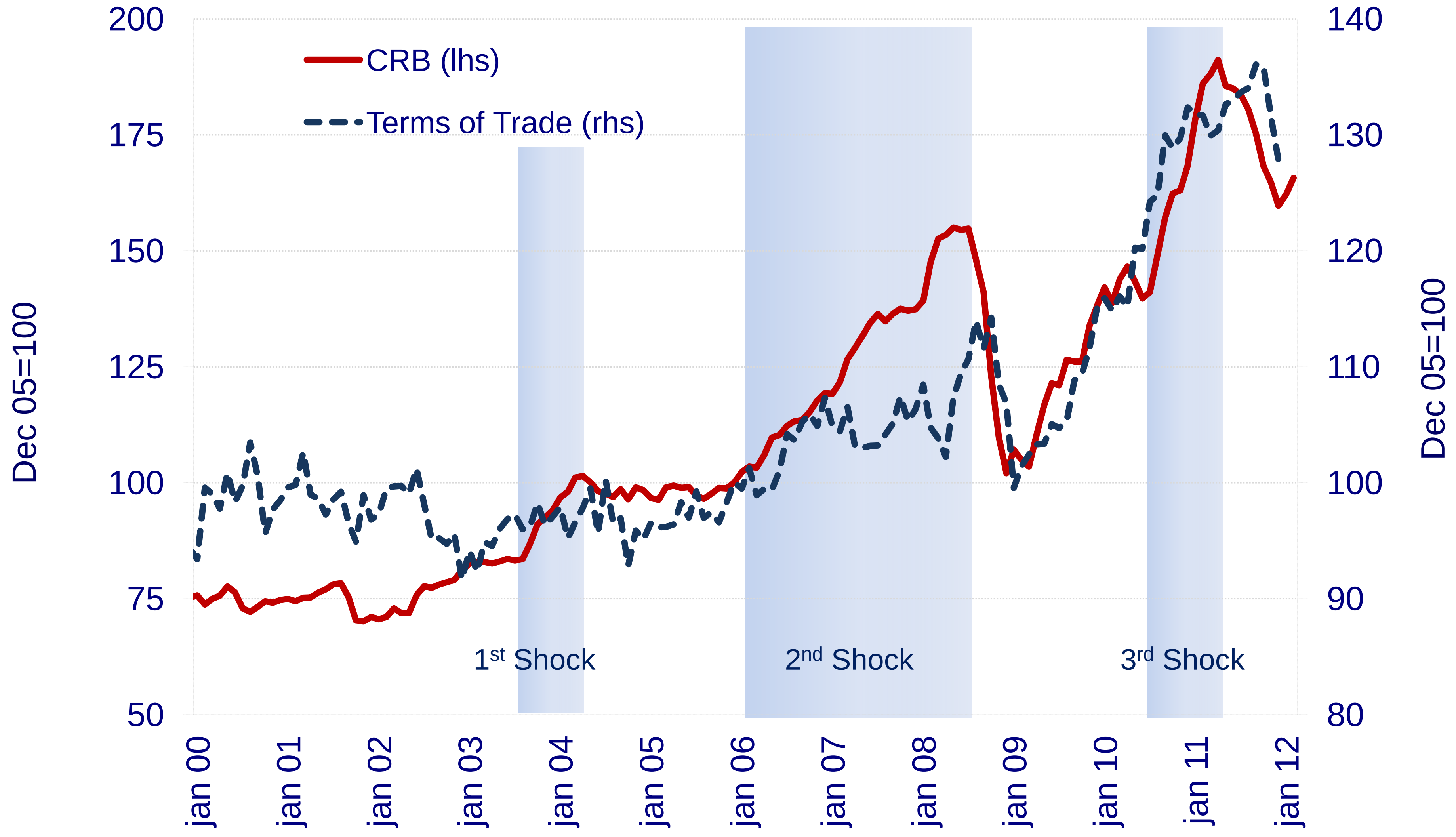
data until Feb 12

Commodity Prices and Inflation



Source: BCB

Commodity Prices and Terms of Trade



Source: BCB

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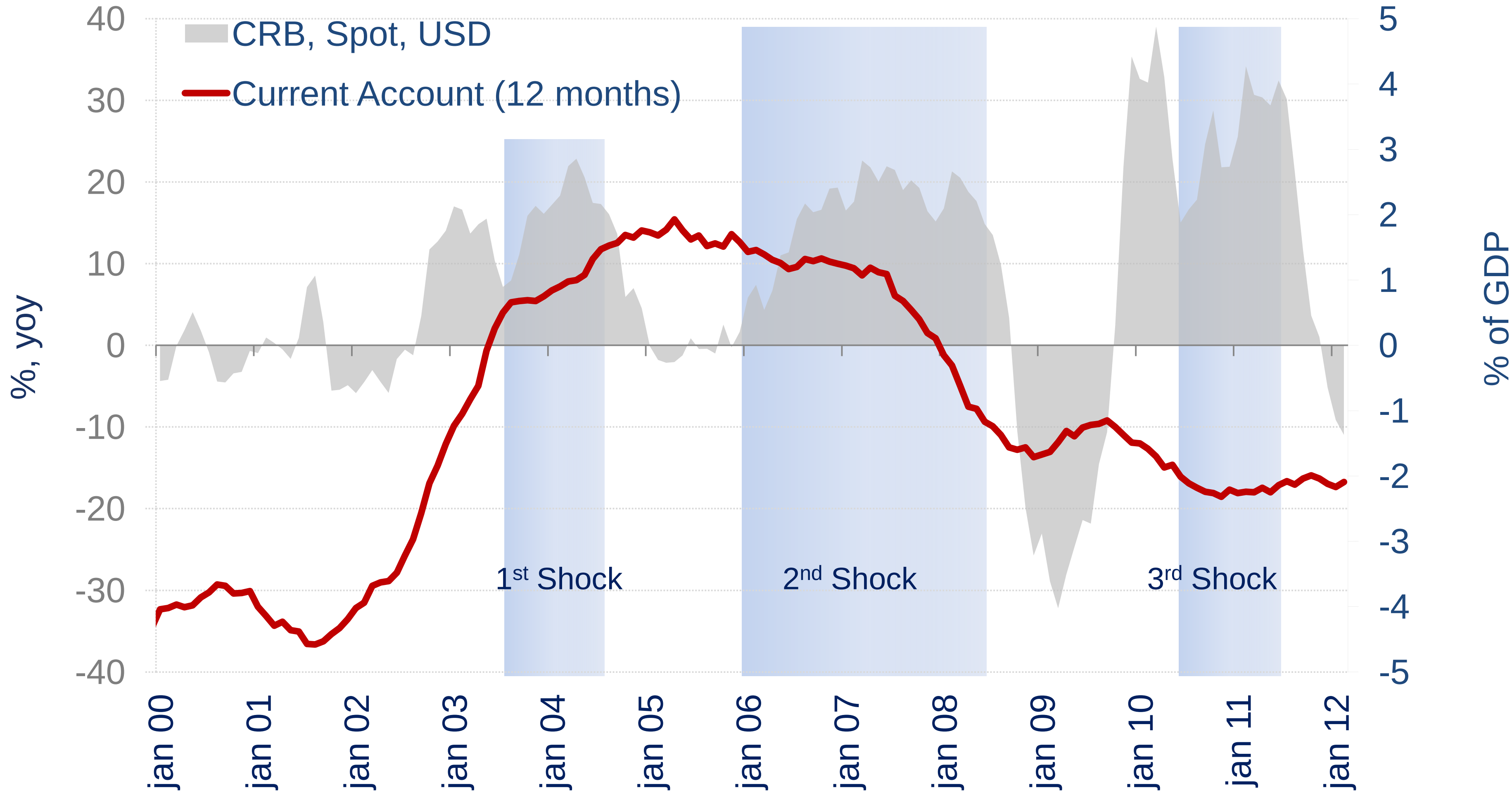
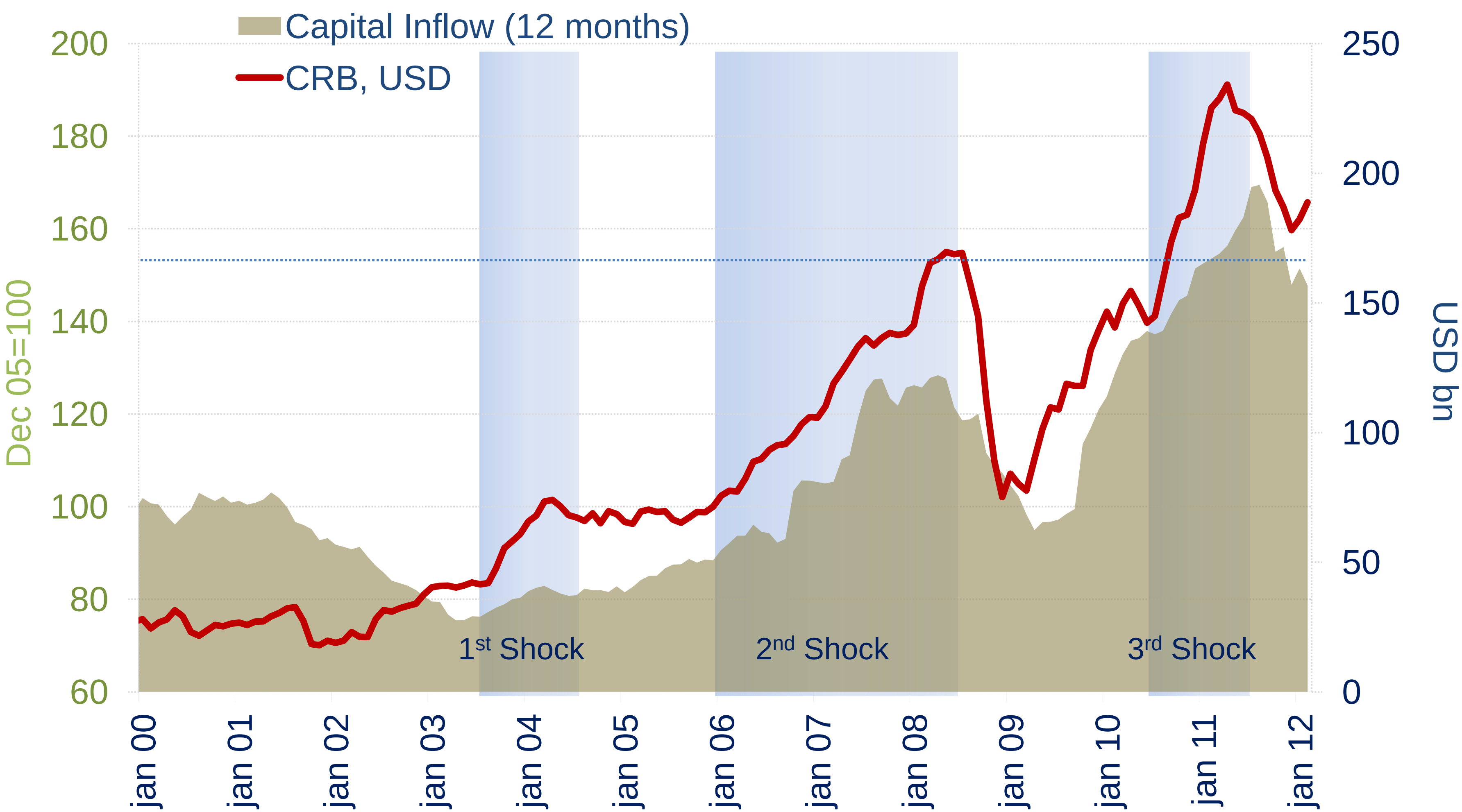
Commodity Prices and Current Account



Source: BCB

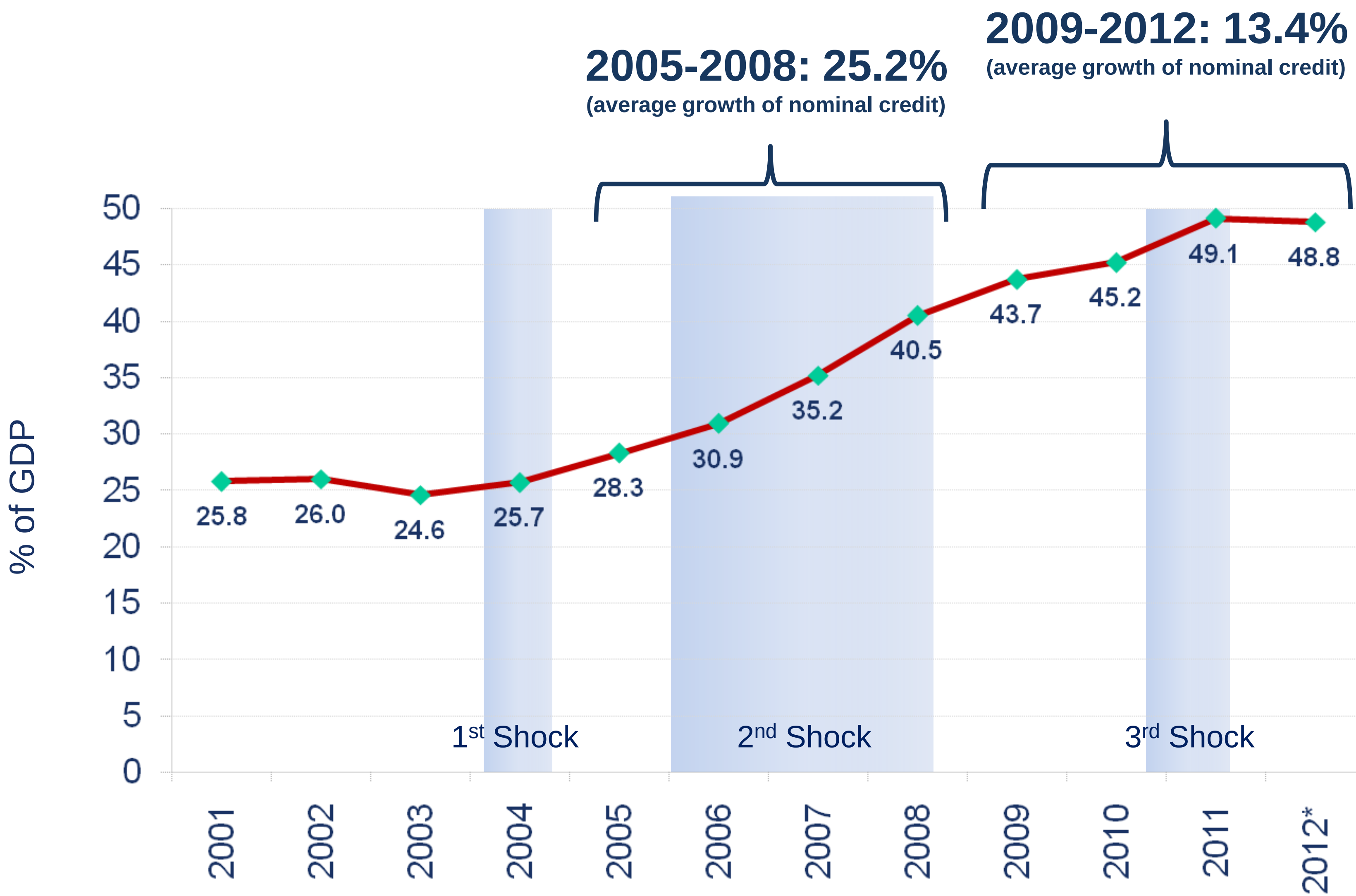
Commodity Prices and Capital Inflow*



Source: BCB

* net portfolio, credit and fdi flows

Commodity Prices and Credit



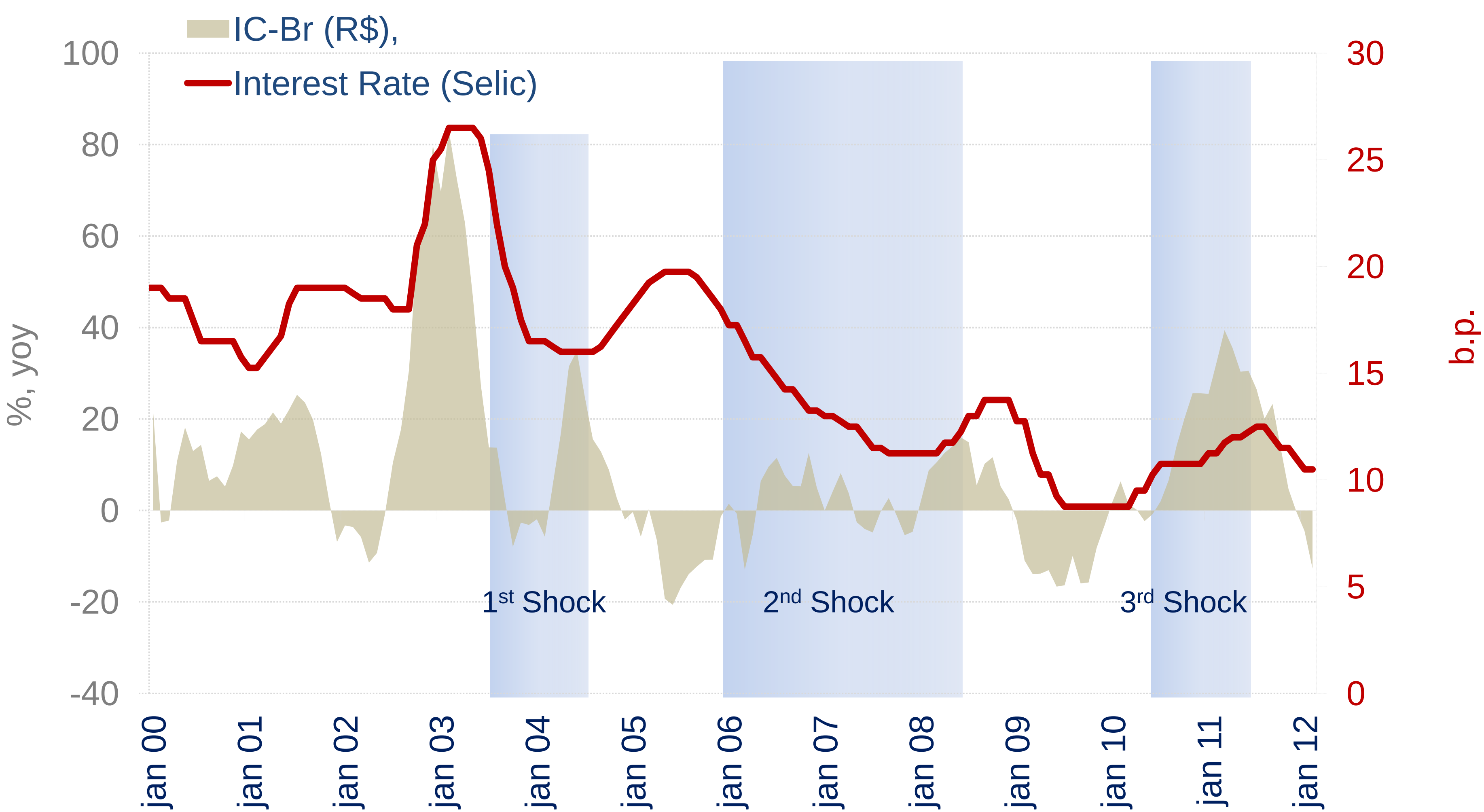
*Fev 12

Source: BCB

Monetary Policy Response

- Accommodation of first round effects
- Combat second round effects
  - Expectations
  - Indexation

Interest Rate Response



Source: BCB

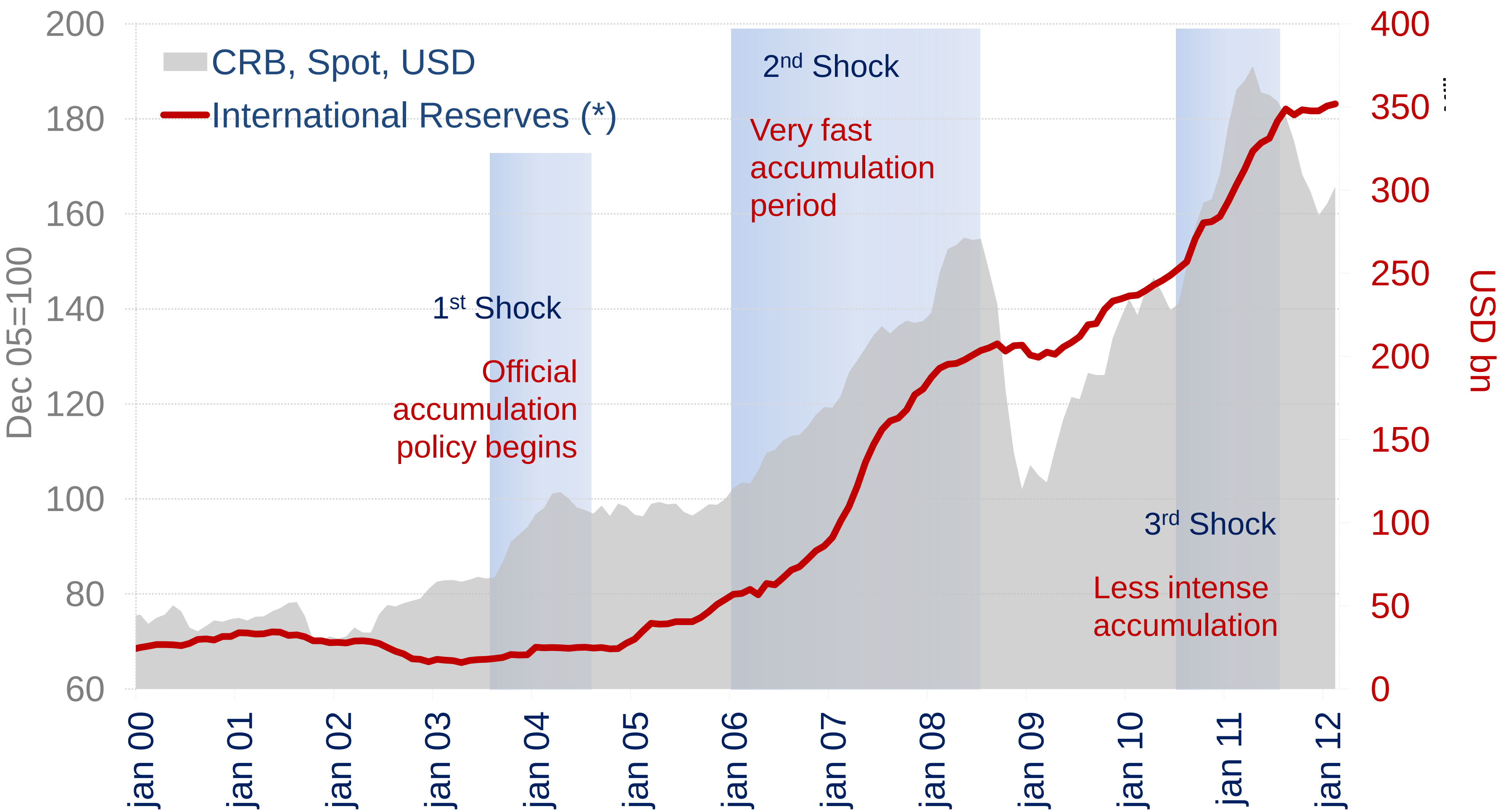
Other Policy Responses

- Fiscal Policy
- International Reserve Accumulation
- Exchange Rate Appreciation
- Macroprudential Measures

Fiscal Policy

Source: BCB

International Reserves



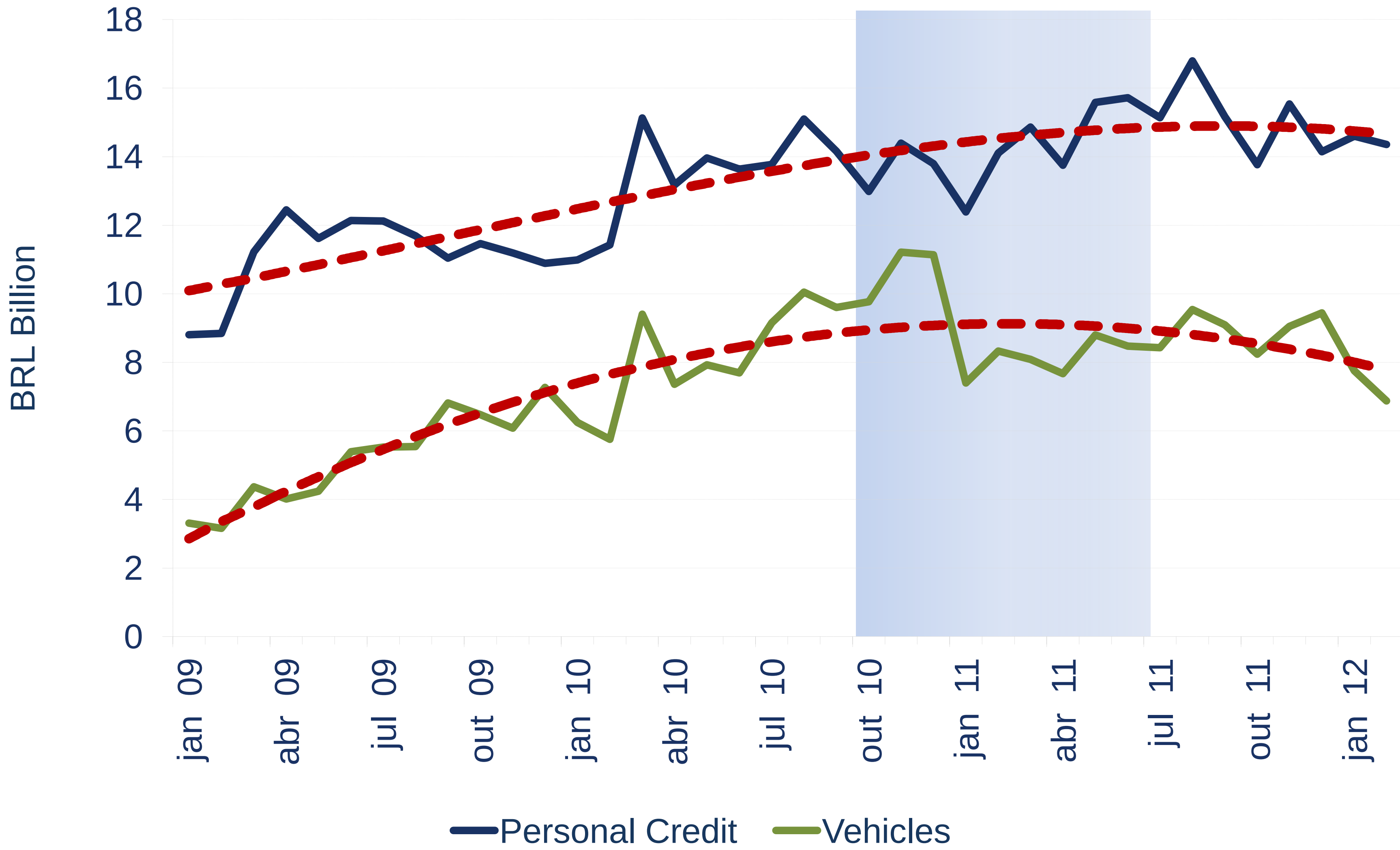
Source: BCB

(*) without IMF liabilities, available as reserves until 2006

Exchange Rate

Source: BCB

Macroprudential - Credit



Source: BCB

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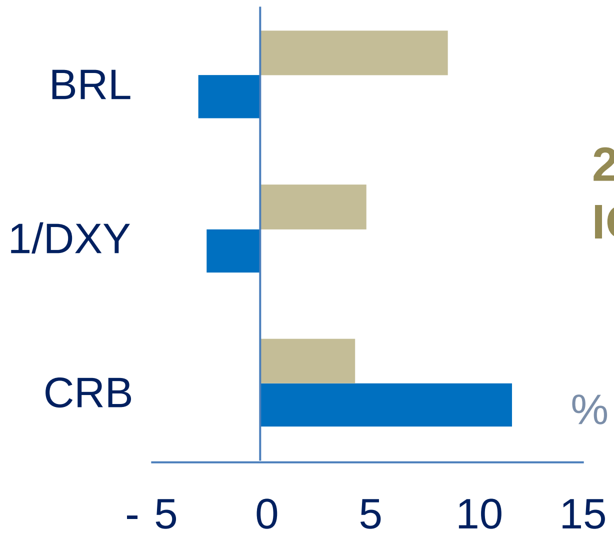
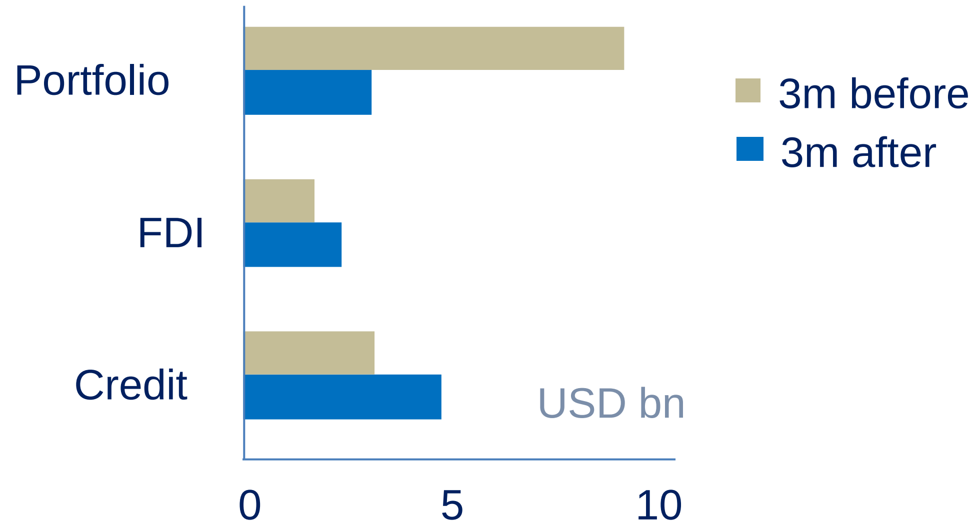
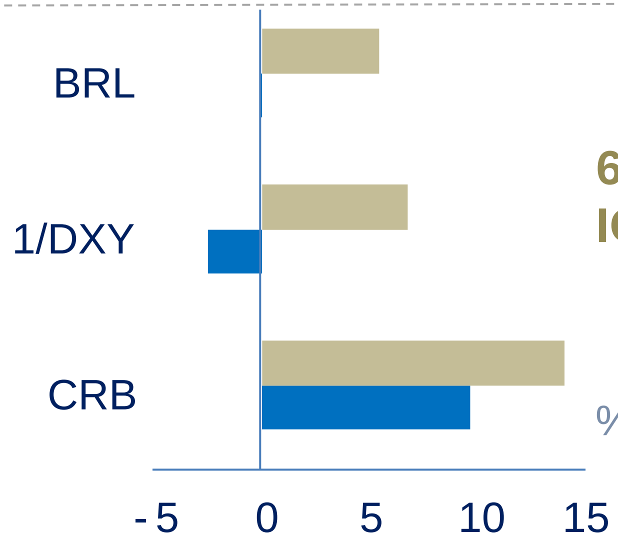
Macroprudential - Capital Flows

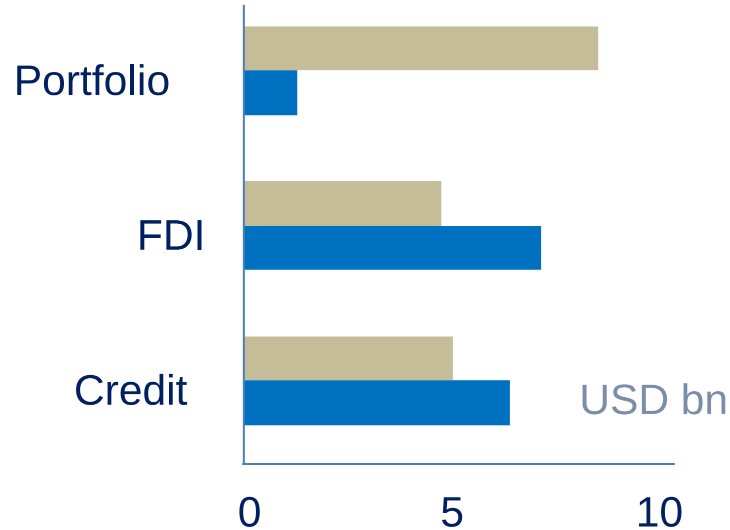


2% IOF





6% IOF



Source: BCB

Summary – Shocks Characterization

- In general, commodity shocks have represented a source of inflationary pressures and improved terms of trade
- These shocks have also been associated with high capital inflows and fast credit expansion

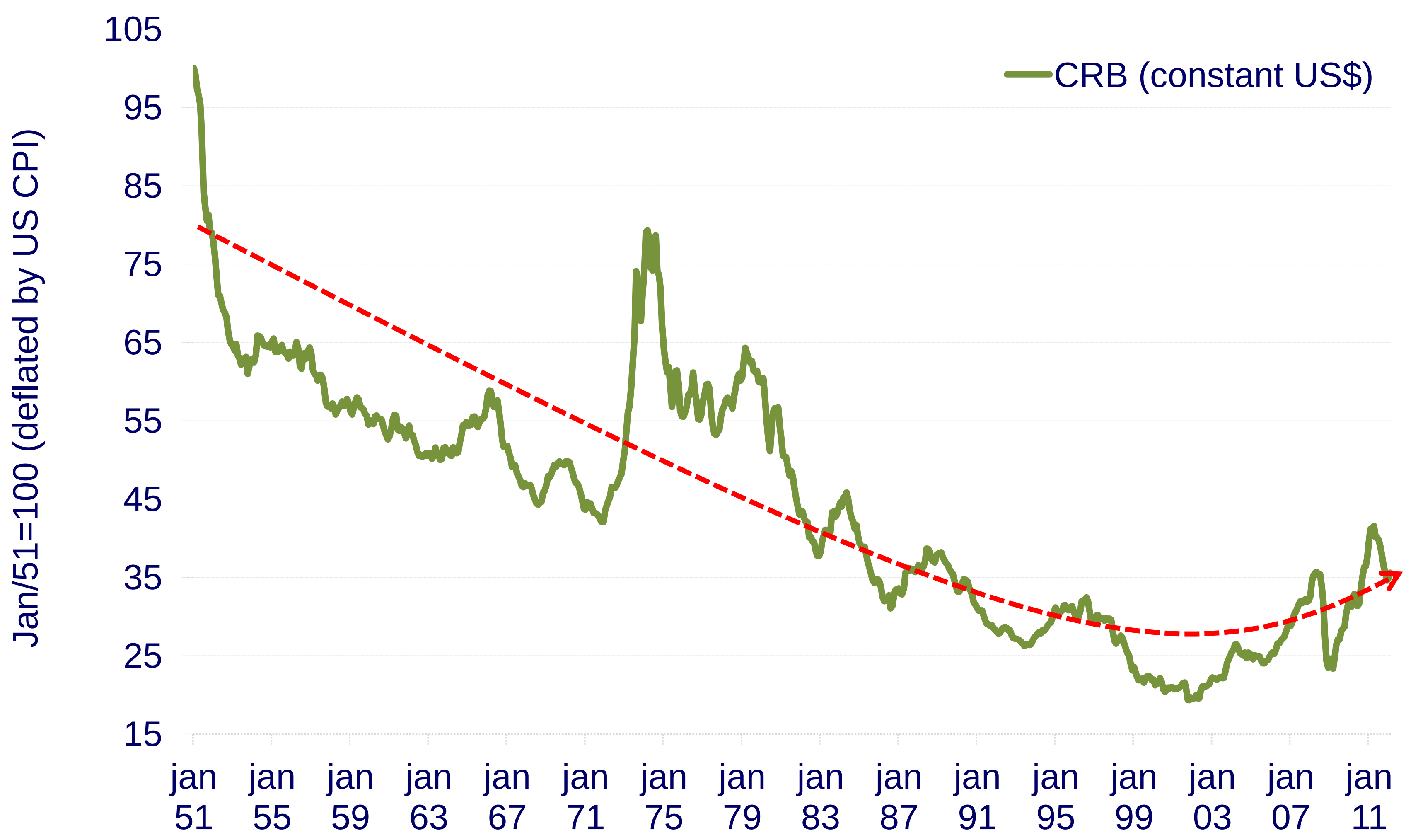
Summary – Policy Responses

- 1st shock (2003/2004): The previous partial reversion of the exchange rate overshooting and tight fiscal stance helped monetary reaction

- 2nd shock (2006/2008): The response encompassed exchange rate appreciation, international reserves accumulation and monetary reaction

- 3rd shock (2010/2011): Excessive credit growth and short-term capital inflow, less scope for appreciation and reserve accumulation paved the way for the introduction of macroprudential measures, to complement fiscal and monetary actions

Commodity Prices in the Longer Run



Source: Thomson Datastream **data until Feb 12**

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