BANCO CENTRAL DO BRASIL

Minutes of the 149th Meeting of the Monetary Policy Committee (Copom)

Date: March 16th, from 4:20PM to 6:00PM, and March 17th, from 4:20PM to 7:25PM
Place: BCB Headquarters meeting rooms - 8th floor on March 16th and 20th floor on March 17th – Brasília – DF

In attendance:
Members of the Committee
Henrique de Campos Meirelles – Governor
Aldo Luiz Mendes
Alexandre Antonio Tombini
Alvir Alberto Hoffmann
Anthero de Moraes Meirelles
Antonio Gustavo Matos do Vale
Carlos Hamilton Vasconcelos Araújo
Mário Magalhães Carvalho Mesquita

Department Heads (present on March 16th)
Adriana Soares Sales – Research Department (also present on March 17th)
Altamir Lopes – Economic Department
João Henrique de Paula Freitas Simão – Open Market Operations Department
José Antonio Marciano - Department of Banking Operations and Payments System
Márcio Barreira de Ayrosa Moreira – International Reserves Operations Department
Renato Jansson Rosek – Investor Relations Group

Other participants (present on March 16th)
Alexandre Pundek Rocha – Advisor to the Board
Eduardo José Araújo Lima – Deputy-Head of the Research Department
Fabio Araujo – Advisor to the Research Department
José de Ribamar Oliveira Júnior – Press Secretary
Katherine Hennings – Advisor to the Board
Ricardo Franco Moura – Advisor to the Board

The members of the Monetary Policy Committee analyzed the recent performance of and the prospects for the Brazilian economy and for the international economy, under the monetary policy framework, which is designed to comply with the inflation targets established by the government.

Recent Economic Developments

1. IPCA inflation strongly accelerated from 0.37% in December to 0.75% in January and 0.78% in February. As a consequence, inflation accumulated in the first two months of 2010 reached 1.54%, 0.5 p.p. above the level registered in the same period of the previous year. The acceleration of inflation in 2010 under this criterion mirrors both the behavior of market prices and of regulated prices. Focusing on market prices, both prices of tradable goods and non-tradable goods accelerated in the first two months, reaching 0.94% and 2.30%, respectively, up from -0.09% and 2.08% in the same period of 2009. On the other hand, the prices of services, whose dynamics tends to show more persistence than that of the prices of goods, decreased from 2.56% in the first two months of 2009, to 2,43% in the same period of 2010. Preliminary data for March point to consumer inflation below that observed in January and February. In short, information available suggests deterioration of inflation dynamics at the margin.

2. The three main underlying inflation measures calculated by the BCB showed divergent behavior between December and February. The core inflation by exclusion increased from 0.46% in December, to 0.59% in January and 0.68% in February. Smoothed trimmed means and double weight core inflation measures accelerated in January and retreated in February (from 0.42% and 0.47% in December, to 0.48% and 0.60% in January, and 0.39% and 0.47% in February, respectively). The twelve-month trailing inflation measures changed from 4.73%, 4.36% and 4.74% in December, to 4.86%, 4.52% and 4.93% in February, for the core inflation by exclusion, smoothed and double weight trimmed means core inflation, respectively. Note that all core measures continued to increase, according to twelve-month trailing inflation, compared to local record lows observed in October and two of them are above the inflation target. Moreover, it bears emphasizing that the behavior of the IPCA diffusion index increased from 60.2% in December 2009 to 61.7% in February (compared to 58.1% in February 2009).

3. The General Price Index (IGP-DI) inflation increased 1.01% in January and 1.09% in February, up from -0.11% in December. In the year through February, the IGP-DI inflation reached 2.11% (-0.12% in the first two months of 2009). Under this comparison basis, the acceleration of the IGP-DI reflected the behavior of its three components. The Wholesale Price Index (IPA-DI), increased from -0.64% in the first two months of 2009 to 2.35% in the same period of 2010. On its turn, the Consumer Price Index-Brazil (IPC-Br) increased 1.98% in the same period (1.05% in 2009). Still according to the same comparison basis, the Civil Construction National Index (INCC) increased 1.00% (0.60% in the first two months of 2009). Regarding the IPA-DI, the inflation acceleration, under this comparison basis, derives basically from the behavior of industrial prices. While the agricultural IPA increased 1.14% (1.70% in the first two months of 2009), the elevation of wholesale industrial prices reached 2.74% (-1.45% in the first two months of 2009). As mentioned in previous Copom Minutes, the Copom evaluates that the effects of wholesale prices over consumer price inflation will depend on current and prospective demand conditions and price-setters' expectations for the future inflation path.

4. The IBGE (Statistics and Geography Brazilian Institute) released information about 2009Q4 GDP and a review of previous data. The data showed expansion in activity, which increased 4.3% in the fourth quarter, year-over-year, and a 2.0% increase quarter-over-quarter, according to seasonally adjusted data. On the aggregate demand side, household consumption and public administration consumption increased, respectively, 7.7% and 4.9%, year-over-year. Gross fixed capital formation (FBCF) increased 3.6% and imports grew 2.5%, according to the same comparison basis, whereas exports declined 4.5%. The positive contribution of domestic absorption to the Q4 GDP growth totaled 5.2 p.p., year-over-year, overweighting the 1.0 p.p. negative impact exerted by the external sector. On the aggregate supply side, still according to the same comparison basis, the services sector presented the best performance, growing by 4.6%, followed by industry (4.0%) and agriculture, which decreased 4.6% relative to the same period of 2008. The GDP deflator under market prices, on a year-over-year basis, changed from 7.4% at the end of 2008, to 4.8% in the fourth quarter of 2009.

5. On a three-month moving average basis, according to data seasonally adjusted by the IBGE, industrial output remained stable in January, after increasing 0.6% in December and 1.3% in November. Still considering the seasonally adjusted series, according to the month-to-month comparison, after the 0.2% retreat observed in December, industrial output increased by 1.1% in January. On a year-over-year basis, industrial output increased by 16% in January, down from 19% in December. The analysis of the behavior of IBGE industrial output series, and its components, suggests that production experiences expansion at a pace which continues to be influenced by the

international outlook, by business and households' expectations, as well as by the easing of domestic financial conditions, supported not only by traditional sources of credit, but also by the recovery of capital markets and the performance of public financial institutions.

6. Among the use categories, according to data seasonally adjusted by the IBGE, in January it bears highlighting the expansions in intermediate goods production (2.0%), and especially, in durable consumer goods production, strongly influenced by the automotive sector, which increased 8.6%. The non-durable and semi-durable consumer goods production increased 0.4%. Capital goods production, recording a -0.1% rate, accommodated in December and January, after rising 6.2% in November. The recovery in industrial production dynamism, despite initially led by the production of durable goods, has become more widespread than before, reflecting tax exemption measures, currently in reversion process, as well as also the easing in financial conditions and income expansion. The future behavior of industrial production, which should not be uniform over time, will depend on these factors, as well as on the evolution of consumer and businessmen confidence, which should continue to be sources of dynamism, to which will be added the recovery of external demand.

7. Labor market has behaved more favorably, with benign aspects prevailing over signs of loss of strength. The unemployment rate in the six metropolitan regions covered by the IBGE Monthly Labor Survey (PME) changed from 7.4% in November to 6.8% in December, increasing to 7.2% in January (8.2% in January 2009). According to the seasonally adjusted series, the unemployment rate reached 7.5% in January, down from 7.9% in the previous month. Average real earnings increased 1.1% in January, after falling by 0.9% in the previous month. Employment, on its turn, increased by 1.4% in December and by 2.1% in January, year-over-year. As a consequence, real payroll expanded 2.2% in December 2009, and 1.7% in January 2010, year-over-year, continuing to constitute a key driver for domestic demand growth. Still regarding the labor market, data from the Ministry of Labor and Employment (MTE) indicate that the formal employment has continued to recover, despite the seasonal job cuts in December. Therefore, 390.8 thousand jobs were created in the first two months of 2010, a record high for the series in this period. The manufacturing industry showed positive balance of 131.9 thousand jobs in the same period, which, together with the services and civil construction, also represented the highest balance registered for the series for this period. The most dynamic sector continues to be civil construction, recording a 12% increase compared to the first two months of 2009.

8. According to data seasonally adjusted by the IBGE, expanded retail sales increased by 0.8% in January, after increasing by 0.6% in December. On a year-over-year basis, the indicator increased 10.3% in January. The three-month moving average of expanded retail sales reached 0.4% in January, according to seasonally adjusted data, after remaining stable in December. On a month-on-month basis, according to seasonally adjusted data, it bears emphasizing the expansion in the sales of "furniture and appliances" (7.9%) and "office material and equipment" (5.8%). Expanded retail sales data have been evidencing growth, mainly influenced by the increase in the sales of durable goods, in response to temporary sector incentives granted by the government, to the improvement in the access to credit supply and to income expansion. For the next quarters, the retail sales trajectory will continue to be sustained by fiscal transfers, as well as by real payroll growth, but it will also be affected by the recovery in the access to credit and by the evolution of consumer confidence.

9. The installed capacity utilization rate (Nuci) in the manufacturing industry, calculated by FGV, without seasonal adjustment, reached 83.1% in February, 6.1 p.p above the level registered in the same month of 2009. According to the CNI series seasonally adjusted by the BCB, the Nuci changed from 81.9% to 81.8%, between December and January. Considering the monthly series with seasonal adjustment, the Nuci calculated by FGV reached 84.0% in February (83.8% in the previous month), above the average observed in the last five years. Similarly, the Nuci in the consumer goods, construction material and capital goods industries in February stood, in the same order, 4.8 p.p., 3.4 p.p. and 4.4 p.p. above the respective averages for the historical series. The Nuci in the intermediate goods industry stood 1.7 p.p. above the same historical average. The reduction of the idle capacity has been led by the expansion in economic activity, not totally offset by the maturity of investment projects. On its turn, data regarding the absorption of capital goods showed recovery compared to the same periods of 2009 and decline at the margin in January month-on-month, after four consecutive months of expansion, accumulating a 17.1% increase. The absorption of capital goods decreased 1.6% in January, according to seasonally adjusted data, a 13.2% increase in year-over-year terms, but an 11.8% decrease in the last twelve

months. On its turn, the production of construction inputs remained stable at the margin in January, after increasing by 1.4% in December. According to observed data, it recorded a 10.8% increase in January 2010, in year-over-year terms, accumulating a 4.7% fall in the last twelve months. In short, evidences suggest that the utilization rates have been increasing in the last months, showing reduction in any remaining idle margin of the industry, despite the recovery of investments. As stressed in previous Copom Minutes, the inflation trajectory is closely linked to current and prospective developments related to the expansion of supply of goods and services to adequately meet demand conditions.

10. The twelve-month cumulative trade balance retreated at the margin, reaching a US$25.3 billion surplus in December, and decreasing to US$24.3 billion in February. This total resulted from US$157.1 billion in exports and US$132.8 billion in imports, equivalent to -17.8% and -20.4% changes, respectively, year-over-year. The greater dynamism of domestic demand relative to the external demand contributes to the narrowing of trade surplus. The increase in remittances of profits and dividends has contributed to elevate the twelve-month trailing current account deficit, which reached US$25.4 billion in January 2010, up from US$24.3 billion in December 2009, equivalent to 1.6% of GDP. On its turn, foreign direct investment reached US$24.8 billion in January, equivalent to 1.5% of GDP.

11. The period since the last Copom meeting, after some initial volatility, was marked by the continuity of the normalization process in international financial markets, in an environment with limited perception of systemic risk. These developments can be attributed to some reduction in the concerns regarding fiscal deterioration in some mature economies, notably in Europe, despite the beginning of the reversal of the strong liquidity expansion occurred in 2009, notwithstanding the remaining high degree of uncertainty. Under these conditions, there was some recovery in the demand for risky assets, as evidenced by the behavior of international financial markets. Moreover, in face of fiscal concerns, the focus in the currency market was the depreciation of euro against other currencies.

12. Regarding the global macroeconomic scenario, the current predominant view points to the recovery in 2010 and some acceleration in 2011, in a process where the US, Europe and Japan (G3) would recover some dynamism, but which would continue to be led by emerging economies. The US economy recorded robust growth in the last quarter of 2009, sustained by the recovery of inventories, and the labor market performance showed some improvement. The economic activity in Japan, on its turn, shows signs of consistent expansion, led by exports, especially to Asia. In the Euro Area, where household consumption remains depressed, the recovery in the fourth quarter of 2009 was quite modest. In short, uncertainty regarding the sustainability of consumption expansion in mature economies still remains, in a scenario of withdrawal of economic policy stimuli and modest prospects for credit expansion, but recovery seems to be consolidating. Moreover, in many emerging economies, economic activity seems to have embarked on a consistent path of recovery, showing, in some cases, evidence of heat in the markets of goods, services, production factors and assets. Therefore, inflation record lows in mature economies and major emerging economies have been exceeded. In this context, after a period of aggressive monetary policy easing, in several countries, monetary policy began a phase of stability, whereas those economies that were less impacted by the international crisis and recover more quickly and intensely tend to adopt more restrictive monetary policy stance.

13. Oil spot prices have increased since the last Copom meeting. Future markets have increased as well. Uncertainty concerning these quotations remains high, as the prospective scenario depends on the evolution of demand, in a context of global economic recovery, on the prospects for the evolution of global supply, subject to the pace of investment maturation in the sector, in addition to the geopolitical issues that affect the price of this commodity. Nonetheless, despite the high uncertainty inherent to the projections regarding the trajectory of oil prices, the main scenario adopted by the Copom assumes unchanged domestic gasoline prices in 2010. However, it bears highlighting that, regardless the behavior of domestic gasoline prices, the evolution of international oil prices can eventually affect domestic prices through productive chains, such as the petrochemical, as well as through the potential effect over inflation expectations. It bears emphasizing that agricultural commodity prices, which have particularly important impact on the evolution of food costs, such as wheat, soybeans and corn, have presented stability since the last Copom meeting. The same behavior was recorded for industrial commodities prices, except for nickel, which have notably increased.

Assessment of Inflation Trends

14. The identified shocks and their impacts were reassessed according to newly available information. The scenario considered in the simulations was based in the following assumptions:

a) the projected adjustments for gasoline and bottle gas prices for 2010 were kept unchanged at 0%;
b) the projected adjustments for fixed telephone and electricity prices for 2010 were kept unchanged at 1.6% and 3.3%, respectively;
c) the projection for regulated prices inflation for 2010, based on individual items, was kept unchanged at 4.0%. This set of prices, according to data released by the IBGE, corresponded to 29.70% of the total February IPCA;
d) the projection for regulated prices inflation for 2011 increased from 4.1% to 4.4%, on the benchmark scenario. Such projection is based on the endogenous determination model for regulated prices, which computes, among other factors, seasonal components, foreign exchange rate changes, market prices inflation and the IGP (General Price Index) change; and
e) the projection for the spreads over the Selic rate, based on the 360-day swap rates, on the benchmark scenario, estimates 35 bps and 42 bps spreads in the fourth quarters of 2010 and 2011, respectively.

15. Regarding fiscal policy, projections assume the achievement of a public sector primary surplus target of 3.3% of GDP in 2010. This percentage can be adjusted by the possibility of reduction by up to 1.12 p.p., due to the implementation of the projects linked to the Growth Acceleration Program (PAC), of which 0.44 p.p. refer to amounts to be paid from 2009. Moreover, it is expected that the primary surplus in 2011 would return, without adjustments, to the level of 3.3% of GDP. The additional assumptions considered in the previous meeting remained unchanged.

16. Since the last Copom meeting, the median of the expectations compiled by the BCB’s Investor Relations Group (Gerin) for the 2010 IPCA increased from 4.60% to 5.03%. For 2011, the median of inflation expectations increased from 4.50% to 4.60%.

17. The benchmark scenario assumes the maintenance of the exchange rate at R$1.80/US$1.00 and the Selic rate at 8.75% p.a. during the forecast period. Under this scenario, the projection for the 2010 inflation increased relative to the figure considered in the January Copom meeting, and is significantly above the midpoint of the 4.50% target established by the National Monetary Council (CMN). According to the market scenario – which incorporates the consensus exchange and Selic rates trajectories collected by Gerin on the eve of the Copom meeting - IPCA inflation forecast for 2010 increased, also standing significantly above the inflation midpoint target. For 2011, under the benchmark scenario, the projection increased relative to the figure considered in the January Copom meeting, and therefore, is above the inflation midpoint target. In the same direction, the projection under the market scenario increased and stands around the midpoint target.

Monetary Policy Decision

18. The Copom evaluates that the monetary policy should contribute to the consolidation of a favorable longer-term macroeconomic environment. In international markets, risk aversion has shown cooling since the last Copom meeting, in a context of abundant liquidity. Under this environment, both Brazilian asset prices, which had also been favoring the easing of domestic financial conditions, as well as the prices of some selected commodities, showed recovery. So, it bears emphasizing that the prospects for foreign funding of Brazilian economy remain favorable. On the other hand, the trajectory of price indices evidences the resumption of external inflationary pressures. Consequently, the benign impact of the international scenario over the domestic inflation path could come to an end, in light of the persistence of uncertainty regarding the behavior of asset and commodities prices in the context of gradual normalization of international financial conditions. The Copom emphasizes that the main challenge of monetary policy in such context is to ensure that the favorable results obtained over the last years are preserved.

19. The Copom believes that, with the confirmation of the incipient evidences of intensification of domestic demand pressures over the market of factors, the probability that initially localized inflationary episodes pose risks to the inflation trajectory increases. In this context, the risk of pass-through of wholesale price upward pressures to consumer prices increases as well. The Committee judges that the materialization of this pass-through, as well as the spread of initially localized pressures over consumer prices, continues to depend critically on the economic agents' expectations for inflation and on the idleness degree of the economy, among other factors. Therefore, these and other variables are part of the information that is taken into account in the generation of the inflation forecasts of the BCB, which constitute a central element in the Committee's assessment on the prospective inflation scenario. Additionally, it should be noted that the behavior of domestic demand tends to exert some pressure over the prices of non-tradable items, such as services, in the upcoming quarters. In any event, the Committee reaffirms that it will continue to conduct its actions to ensure that the gains obtained in inflation control in recent years become permanent.

20. The Copom considers important to emphasize, once more, that there are important time lags between the implementation of monetary policy and its effects on both economic activity and inflation. Therefore, the assessment of alternative options for monetary policy should necessarily focus on the forward-looking inflationary scenario and its risks, which suffered some deterioration in recent months, instead of current inflation figures. The Committee reaffirms that specific asset price movements are only relevant for monetary policy if they impact the forward-looking inflationary path.

21. Prospects for the evolution of domestic economic activity remain favorable, as evidenced by data on trade, manufacturing capacity utilization and the labor market, as well as by signs of continued expansion of credit supply, both for individuals and corporate. It should be noted that consumers and businessmen confidence is at historically high levels. Under these circumstances, the pace of activity depends significantly upon the evolution of real earnings, the effects of fiscal stimulus measures and the increments of governmental transfers that will occur in the upcoming months. The dynamism of activity should also be benefited by the easing of financial conditions, favored, among other factors, by the policies of official banks. In short, the most recent data on domestic economic activity reinforce the assessment mentioned in previous Copom Meeting Minutes that the contractionist influence of the international financial crisis over the domestic economy dynamism and, consequently, over the context on which monetary policy operates, could become persistent, but would not be permanent. These considerations become even more relevant considering the fact that the current monetary policy decision will have more impacts from the middle of 2010 on.

22. The Copom believes that the main risks to the consolidation of a benign inflationary scenario stem, regarding the external outlook, from a possible rise in commodity prices and, regarding the domestic scenario, from the cumulative and lagged effects of the financial conditions easing and the fiscal and credit impulse over the evolution of domestic demand, taking into account the dynamics of consumption and investment, in the context of the rapid reduction in the idleness margin in the use of production factors. The balance of these influences on the future trajectory of inflation will be crucial for the assessment of the different monetary policy stances.

23. International evidence, as well as the Brazilian experience, indicates that high inflation rates lead to the increase of risk premium, for both private and public funding, to the shortening of planning horizons and, consequently, to lower potential economic growth, besides having regressive effects over income distribution. Therefore, the Copom strategy aims to ensure that the convergence of inflation towards the targets path observed in 2009 continues to be registered in 2010 and 2011. This implies that possible deviations from the target path be promptly corrected. Such strategy takes into account the time lags in the transmission mechanism and is the most adequate to deal with the uncertainty inherent to the process of monetary policy formulation and implementation.

24. The Committee considers that the accommodation of demand, driven by the tightening of financial conditions and the deterioration of the agents' confidence, as well as by the contraction of the global economy, was overcome. Therefore, it is reasonable to affirm that the economy is already in an expansion cycle, while there is still uncertainty to be resolved over time about the pace of this process. Under this scenario, which is supported by the data available so far, monetary policy must ensure inflationary pressures remain contained.

25. In short, the Committee evaluates that, given the signs of strength in domestic demand, resulting in the reduction in the idleness margin of the production factors, as evidenced by indicators of manufacturing capacity utilization and labor market, and by the recent behavior of inflation expectations, the risks to the achievement of a benign inflationary scenario, in which inflation would remain consistent with the inflation targets, have increased. Under this environment, monetary policy should remain especially vigilant in order to avoid that the greater uncertainty detected in shorter horizons spread to longer horizons.

26. In light of these considerations, there was consensus among committee members about the need to implement an adjustment in the basic interest rate, in order to contain the gap between the pace of domestic demand and productive capacity, as well as to strengthen the anchoring of inflation expectations.

27. Under these circumstances, the majority of the Committee members, in light of information available at the moment, considering the fact that the process of withdrawal of stimuli introduced during the crisis has already begun, evaluated that it is more prudent to await the evolution of the macroeconomic scenario until the next meeting, so that to start the adjustment of the basic interest rate. On the other hand, the other Committee members, who understood that inflation projections and the balance of risks would support the beginning of the adjustment already at this meeting, voted for an immediate 50-bps increase in the basic interest rate.

28. Under this context, assessing the macroeconomic outlook and the inflation prospects, the Copom decided to maintain the Selic rate at 8.75% p.a., without bias. Five votes were for the monetary policy action, and three votes were for 50-bps increase in the Selic rate. The Committee will carefully monitor the evolution of the macroeconomic scenario until its next meeting, in order to define the next steps in its monetary policy strategy.

29. Under the inflation-targeting regime, the Copom guides its decisions according to projected inflation, the analysis of several alternative scenarios for the evolution of the main variables that determine the forward-looking dynamics for prices, and the balance of risks associated to the projections. After a brief contraction, domestic demand recovered, largely thanks to the effects of stimulus factors, such as income growth and credit resumption. On its turn, important fiscal and credit incentives have been provided to the economy in recent quarters, and should contribute for the consolidation of activity resumption and hence, for the reduction of any residual idleness margin of productive factors. The effects of these stimuli will be an important part of the context in which future decisions on monetary policy, which must ensure the maintenance of inflation convergence to the targets path in 2010 and 2011, will be taken.

30. In addition, it bears noticing that there was also consensus among the Committee members about the need to adapt the pace of adjustment of the basic interest rate to the developments in the prospective inflation scenario, as well as to the corresponding balance of risks, in order to limit the impacts caused by the behavior of current inflation over the underlying prices dynamics.

31. At the end of the meeting it was announced that the Committee will reconvene on April 27th, 2010 for technical presentations and, on the following day, to discuss the monetary policy decision, as established in Communiqué 18,927 of October 9th, 2009.

SUMMARY OF DATA ANALYZED BY THE COPOM

Inflation

32. The IPCA rose 0.78% in February, up from 0.75% in January, the largest increase since May 2008. Considering the last twelve months, the index increased 4.83%, up from 4.59% in January. The annual adjustment of school fees contributed, individually, with 0.32 percentage points, constituting the greatest impact on the IPCA result, in February. Food and beverages, and transportation, which have higher weights in the index, also recorded above-the-average monthly increases, despite their deceleration when compared to changes observed in January.

33. The increase in market prices rose from 0.72% in January to 0.93% in February, mainly driven by the higher change recorded by non-tradable goods, 1.54%, up from 0.75% in the previous month, while the prices of tradable goods increased 0.26%, down from 0.68% in January. Regulated prices increased 0.42%, down from 0.83% in January, mainly reflecting the lower impact of public transportation adjustments. In the last twelve months through February, market prices rose 4.77%, and regulated prices increased 4.97%, against 4.50% and 4.82% in January, respectively. The diffusion index stood at 61.7% in February, down from 68.7% the previous month.

34. The IPCA-EX core, which excludes all fuel items and ten items of household food, accelerated in the month, from 0.59% to 0.68%. In twelve months, it slightly decelerated, reaching 4.86% in February, down from 4.87% in January. The smoothed trimmed-mean core measure increased 0.39% in February, down from 0.48% in January, increasing by 4.52% in twelve months, compared to 4.41% in the previous month. The double weight core increased by 0.47% in the month, down from 0.60% in January, increasing 4.93% in twelve months, down from 4.96% in January.

35. The IGP-DI increased by 1.09% in February, after rising 1.01% in January, with increase in wholesale prices (IPA) and deceleration in consumer price inflation (IPC) and construction prices (INCC). The IGP-DI expanded by 2.11% and 0.77% in the year and twelve months, respectively. The IPA-DI increased 1.38% in the month, up from 0.96% in January, an increase both in agricultural prices, 1.46%, and in industrial products, 1.35%. In the year, the IPA-DI increased 2.35% and in twelve months, -1.19%. The IPC-DI rose 0.68% in February, down from 1.29% in January, increasing by 1.98% in the year and 4.91% in twelve months, with deceleration in five of seven groups that compose it. The INCC-DI increased 0.36%, down from 0.64% in the previous month, with highlights to the smallest change in the prices of the labor force, which increased 0.21%, down from 0.68% in January. In the year and twelve months, the index expanded by 1.00% and 3.66%, respectively.

Economic Activity

36. GDP grew 2% in 2009Q4, quarter-over-quarter, down from 1.7% in 2009Q3, according to seasonally adjusted data from the IBGE’s Quarterly National Accounts of the IBGE. The result reflected respective expansions of 4% and 6% in the performance of industry and services sector, while agricultural production remained stable in the period. On the demand side, 2009Q4 GDP growth was led by investment, with a 6.6% increased in the fixed capital gross formation, according to the same comparison basis. Household and government grew 1.9% and 0.6%, respectively, confirming the importance of the contribution of domestic demand for greater dynamism of economic activity in the period. Despite the recovery since the second quarter of 2009Q2, GDP fell by 0.2% in the year.

37. Expanded retail sales increased 0.8% in January, month-on-month, after rising 0.6% in December and falling 0.3% in November, according to seasonally adjusted data by the IBGE’s monthly survey (PMC). The average sales for the quarter ended in January rose 0.7%, compared to the quarter ended in October. Expanded retail sales grew 10.3%, year-over-year, increasing by 7.4% in the last twelve months through January. All ten sectors surveyed reported increases month-on-month, with highlights for furniture and appliances, 7.9%, and equipment and office supplies, 5.8%.

38. Year-over-year, all commerce segments expanded, with highlights to the increases in the sales of equipment and office material, 32.2%, and furniture and appliances, 17.7%. In the last twelve months, there were increases in eight of the ten sectors surveyed, with emphasis on the growth in pharmaceutical and medical articles and vehicles and motorcycles, parts and pieces, both recording 11.9%. Among the segments that presented negative performance, according to the same comparison basis, it bears noticing construction materials, -5%, and textiles, clothing and footwear, -2.2%.

39. Data from the São Paulo Trade Association (ACSP), covering the state capital, showed increases of 1.2% in the number of consultations to the Central Credit Protection Service (SCPC) and 1.6% to the Usecheque system, in February, according to the month-on-month seasonally adjusted series. In the year through February, these indicators increased 3.9% and 4.9%, respectively, relative to the same period last year.

40. Automobile sales by dealers, including cars, light commercial vehicles, trucks and buses, rose 6.9% in February month-on-month, according to Fenabrave (Brazilian Federation of Automotive Vehicles Distribution) data,

seasonally adjusted by the BCB. The increase in the month reflects mainly the performance of car sales, 6.7%, followed by light commercial vehicles, 0.9%, while buses and trucks sales decreased 17% and 10.3%, respectively. It should be noticed that the push in car sales in February also reflected the proximity to the closing date for the sale of flex-fuel vehicles with discounted tax over industrialized products (IPI), which will take place in March. Total sales increased 10.8% year-over-year, with emphasis on the growth of trucks (23.6%) and light commercial vehicles (17.5%).

41. Capital goods imports decreased 8.1% in January, month-on-month, according to the Funcex quantum index, seasonally adjusted by the BCB. The January indicator increased 7% year-over-year, reaching an 11.6% decline in the last twelve months through January, compared to the same period last year.

42. Capital goods production decreased 0.1% in January, month-on-month, and expanded 12.8% year-over-year, according to IBGE's seasonally adjusted data. Month-on-month, it bears highlighting the fall in production of capital goods for construction, -13.9%, for agricultural use, -8.9% and for non-serial industrial use, -4.3%. Compared to the same period of 2009, it bears noticing the production of capital goods for construction, which increased 202.6%. The production of construction inputs remained stable month-on-month, and increased 10.8% year-over-year.

43. Industrial production increased 1.1% in January, month-on-month, when it had registered -0.2%, seasonally adjusted, according to IBGE's Monthly Industrial Survey – Physical Production (PIM-PF). Year-over-year, industrial ouput grew by 16%, accumulating a 5% reduction in the last twelve months, over the same previous period. Month-on-month, it bears highlighting in January the expansion in the production of durable consumer goods, 8.6% and intermediate goods, 2%. The production of semi and non-durable consumer goods increased 0.4%. Year-over-year, all use categories expanded, with emphasis on the increase of 36.4% in durable consumer goods and 20.2% in intermediate goods production. In a twelve-month trailing basis, production retreated in the four categories of use, especially in capital goods, falling by 15.8%, followed by intermediate goods, with retreated 5.9%.

44. Real earnings in the manufacturing industry declined 1.5% in January month-on-month, while in December it expanded by 1.5%, according to data released by the CNI, seasonally adjusted. Despite the decline at the margin, employment and hours worked rose by 2% and 1.3%, respectively, in the same period. Year-over-year, these indicators increased 7.7%, 1% and 3.8%, respectively.

45. According to CNI, the Nuci reached 79.9% in January, 3.6 percentage points higher than the level observed in the same month of 2009. Considering the seasonally adjusted series, the Nuci was 0.1 p.p. below the level recorded in December, but expanded by 1 p.p. in the quarter ended in January. In fourteen out of the nineteen segments of the manufacturing industry, the Nuci presented positive performance month-on-month.

46. According to Anfavea, vehicles production reached 253.2 thousand units in February, increasing by 23.9% year-over-year. According to seasonally adjusted data, vehicles production increased 1.6% in February, month-on-month. In the year and twelve months through February, the production of vehicles increased 28.3% and 6.3% respectively. Domestic sales of vehicles decreased 4.6% in February, month-on-month, while in the year and twelve months through February, it increased 5.7% and 12.2%, respectively, compared to the same periods in 2009. Exports increased 88.3% year-over-year and 102.9% in the year, but decreased 21.2% in the last twelve months.

47. The LSPA survey carried out by the IBGE in February estimated the production of 145.1 million tons in 2010, up from 133.8 million tons in 2009. The new estimate represents an 8.5% increase relative to 2009, with projected expansions of 17.4% and 2.6% for the production of soybeans and corn, respectively. For products directly related to the basic basket, such as rice, beans and wheat, the survey projected changes of -5%, 6.8% and 9.4%, respectively.

Surveys and Expectations

48. According to the Fecomercio-SP survey, the Consumer Confidence Index (ICC) decreased 1.4% in March, month-on-month, when it reached a record high for the series. This result reflected the falls of 1.8% in the

Consumer Expectations Index (IEC) and1.1% in the Current Economic Conditions Index (Icea). Year-over-year, the ICC increased 22.2%.

49. According to the Consumer Expectations Survey carried out by the FGV nationwide, the ICC decreased 2.2% in February, month-on-month seasonally adjusted. In the month, the Current Situation Index (ISA) and the Expectations Index (IE) decreased 0.8% and 3%, respectively. Year-over-year, the ICC increased 15.4%, resulting from the increases of 24.3% in the ISA and of 10.3% in the IE.

50. The Industry Confidence Index (ICI) from FGV reached 115.8 points in February, the highest level recorded since December 2007, standing 1.9% above the level observed in January, according to seasonally adjusted data and 54.3% higher than the level observed in February 2009. By components, monthly increases were recorded for the Current Situation Index (ISA), 0.7%, and for the IE, 3.3%, seasonally adjusted. Year-over-year, expansions of 46.3% and 63.8% were recorded for the same indicators, respectively.

51. According to the CNI survey, the industrial businessmen confidence cooled in February, as evidenced by the Industrial Business Confidence Index (Icei), which fell to 67.8 points, down from 68.7 points registered in January. Despite the fall, related to seasonal aspects, the index remains 9.2 percentage points above the historical average.

Labor Market

52. According to the General Record of Employment and Unemployment (Caged) of the Ministry of Labor and Employment (MTE), 181.4 thousand formal jobs were created in January, a record high for the series for this month, accumulating 1,278.3 thousand hires in the last twelve months. Considering seasonally adjusted data, employment level expanded 0.7% month-on-month. The manufacturing industry outperformed in the month, with the opening of 68.9 thousand jobs. At the margin, employment in the sector grew 0.8%, considering seasonally adjusted data, and 1.9% year-over-year. The service sector created 57.9 thousand jobs in the month, with increases of 0.5% and 4.3% in the employment level, month-on-month and year-over-year, respectively. The construction sector was responsible for the supply of 54.3 thousand jobs during the month, representing growth in the level of employment of 1.5% month-on-month and 11% year-over-year.

53. According to the IBGE employment survey (PME), carried out in the six main metropolitan regions of the country, the unemployment rate reached 7.2% in January, increasing 0.4 p.p. month-on-month and declining 1 p.p. year-over-year. The increase in unemployment in the month resulted from the fall of 210 thousand jobs, higher than the reduction of 115 thousand people in the Economically Active Population (PEA). In seasonally adjusted terms, the unemployment rate fell by 0.4 p.p. in the month and reached 7.5%. According to the survey, average real earnings usually earned by workers increased 1.1% month-on-month after falling 0.9% in December, and decreased 0.4% year-over-year, the first decline recorded according to this basis comparison basis since July 2005. Payroll grew 0.1% month-on-month and 1.7% year-over-year.

Credit and Delinquency Rates

54. Outstanding credit in the financial system reached R$1,422 billion in January, equivalent to 44.6% of GDP, with increases of 0.7% in the month and of 15.7% in the last twelve months. Non-earmarked credit operations increased 0.3% in the month and 9.9% in the last twelve months. Among the non-earmarked operations, credit operations to individuals increased 0.9% in the month and 18.7% in twelve months, while non-earmarked credit operations to corporate decreased 0.3% and expanded 2.4%, according to the same comparison bases. Earmarked credit operations increased 1.7% in January and 29.9% in twelve months, mainly influenced by housing credit and the ones granted by the BNDES, which rose 45.9% and 36.1%, respectively, in the last twelve months.

55. The average interest rate on non-earmarked credit operations, used as reference for interest rates, increased again in January, reaching 35.1%, up from 34.3% the previous month. The average annual rate on credit for individuals reached 43% in the month, up from 42.7% in December, and the average rate on corporate credit increased 26.5%, 1 p.p. above the level recorded in the previous month.

56. The average tenure on non-earmarked credit operations, used as reference for interest rates, increased in January for the fifth consecutive month, reaching 394 days, up from 390 days in December. The average tenure of corporate credit operations reached 288 days, while the average tenure for credit operations to individuals totaled 523 days.

57. Delinquency rates in the financial system (non-earmarked loans used as reference for interest rates, in arrears for more than ninety days) reduced from 5.6% in December to 5.5% in January. Delinquency rates for credit operations with corporate remained stable in 3.8%, and with individuals, declined 0.1 p.p., reaching 7.7%.

58. Net delinquency rate for retail credit, measured by the ACSP, reached 6.3% in February, compared to 5.8% in January and 7.8% year-over-year.

External Environment

59. The set of data released since the last Copom meeting is less clear regarding the support of a steady process of economic growth resumption in 2010. Despite positive results for Q4 GDP in the US, Japan, Euro Area and the United Kingdom, the Japanese figures were revised downwards, and at the Euro area, data showed strong decline quarter-over-quarter. It is noteworthy that significant improvement in domestic demand in Japan results from the consumption of durable goods, especially cars, as a result of fiscal incentives. It also bears emphasizing the deterioration in expectations of European consumers, the contraction in the index of purchases by managers in China, in addition to the reduction in the number of hours worked and weekly earnings in the labor market in the US. In several ways, the Southeast Asian emerging economies continue to gain strength, a scenario that also prevails in commodity exporter countries in Latin America.

60. This recovery environment of emerging economies is supported not only by a pickup in domestic demand, but also by the force of the Chinese economy, to which converges significant share of exports of commodities exports, whose prices continue to grow, after the price correction at the beginning of year. Due to these increases, consumer price indices indicated, in January, annual rises of 8.2%, 1.5%, 16.1%, 4.3% and 8.2%, respectively, in Turkey, China, India, Philippines and Argentina, all of them presenting accelerating trend. The same behavior was observed in the US, Euro Area and the United Kingdom, which recorded 2.6%, 1% and 3.5%, in this order.

61. Despite the exhaustion of the processes of deflation/ disinflation, most central bank believe that inflation expectations remain anchored. As the recovery is still fragile, particularly in mature economies, these central banks have kept the focus on liquidity management, including the closure of programs to increase the liquidity created during the crisis, avoiding, now, an increase in the basic interest rate. Among the central banks of emerging economies, the People's Bank of China raised again the reserve requirements, a process also undertaken by the Reserve Bank of India, while the monetary authority of Malaysia surprised by increasing the interest rate, similar to the action taken again by the Reserve Bank of Australia.

62. Since the last Copom meeting, the major tensions in international economy have stemmed from the risks related to fiscal deterioration, especially in Europe, where uncertainties regarding the ability to rollover short-term debt has increased, particularly in Greece and Portugal, but also in Ireland, Italy and Spain.

Foreign Trade and International Reserves

63. The Brazilian trade surplus reached US$394 million in February, accumulating US$228 million in the year, compared to US$1.2 billion in the same period of 2009. In twelve months, the surplus reached US$24.3 billion, growing 0.3% year-over-year. In the month, exports totaled US$12.2 billion, and imports, US$11.8 billion, growing by 27.2% and 50.8%, respectively, year-over-year, on a daily average basis. External trade reached US$46.8 billion in the year through February, growing by 24.7% relative to the same period of 2009. External trade reached US$ 46.8 billion in the first two months of 2010, growing by 24.7% year-over-year.

64. Based on the liquidity concept, international reserves, which encompass the balance of borrowing operations in foreign currencies, reached US$241.3 billion in February, recording a US$516 million growth month-on-month.

Under the cash concept, international reserves totaled US$241.1 billion, recording a US$599 million increase, according to the same comparison basis. The monetary authority's interventions accounted for net purchases of US$ 433 million in February, with highlights to the acquisitions of US$ 350 million on a cash basis.

Money Market and Open Market Operations

65. In the period following the Copom meeting in January, the slope of the yield curve reduced, with increase in short-term rates and decrease in the rates whose maturities are over one year. In the short-term component of the yield curve, the successive upward revisions in inflation expectations, the disclosure of higher price indices and activity data and employment data, suggesting a consistent recovery of the economy, contributed to this movement. The long-term component of the yield curve was influenced by the expectation of anticipation of the increasing cycle in the basic interest rate and by the inflow of foreign investors. Between January 22nd and March 15th, one- three- and six-month and one-year rates increased by 0.21 p.p., 0.46 p.p., 0.55 p.p. and 0.40 p.p., respectively. The two- and three-year rates decreased by 0.10 p.p. and 0.44 p.p., respectively. Real interest rates, measured by the differential between the one-year forward nominal interest rate and the smoothed twelve-month-ahead inflation expectations, increased from 5.74% on January 22nd to 6.05% on March 15th.

66. In its open market operations, the BCB carried out between January 26th and March 15th, repo operations borrowing R$ 18 billion for a six-month period. As a consequence, the average daily balance of the long operations reached R$ 88.7 billion. In the same period, the BCB also borrowed money through repo operations with tenures between 13 and 33 working days, increasing the average daily balance of short-term borrowing operations to US$318.9 billion. The BCB also borrowed money through 34 overnight repo operations and conducted daily, at the end of day, two-working-day tenure liquidity management operations. The very short-term operations, including the two-working-day tenure liquidity management operations, averaged a daily balance of R$ 80.3 billion in the period. The average daily balance of the total stock of repurchase agreement of the Central Bank decreased from $ 489.8 billion between December 8th 2009 and January 25th 2010 to $ 487.9 billion between January 26th and March 15th. Considering the daily balance of operations for the most recent period, there was a fall in the repurchase agreements totaling R$ 41.0 billion, with a decrease in total stock from R$ 514.3 billion on January 25th to R$ 473.3 billion in March 15th. The main driver of liquidity contraction in the period was the net placement of securities by the National Treasury.

67. Between January 26th and March 15th 2010, the National Treasury issuance regarding the traditional auctions raised a total of R$55 billion. The issuance of fixed-rate securities reached R$30 billion, R$20.7 billion via issuance of LTNs maturing in 2010, 2011 and 2012, and R$9.3 billion via NTN-Fs maturing in 2014, 2017 and 2021. Issuance of LFTs totaled R$10.5 billion, for securities maturing in 2013 and 2015. Issuance of inflation-linked NTN-Bs reached R$14.5 billion, for securities maturing in 2013, 2015, 2020, 2030, 2040 and 2050.