52nd

Minutes of the Meeting of the

Financial Stability Committee — Comef

March 1st and 2nd, 2023

BANCO CENTRAL DO BRASIL

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Date: March 1st and 2nd, 2023

Venue: Meeting rooms on the 8th floor (March 1st) and on the 21st floor (March 2nd)
BCB Headquarters – Brasilia – DF – Brazil

Starting and ending times: March 1st: 9:30 AM – 12:30 PM; 2:30 PM - 5:00 PM
March 2nd: 2:00 PM - 5:00 PM

In attendance:

Members of the Comef

Roberto de Oliveira Campos Neto
Governor

Bruno Serra Fernandes
Deputy-Governor for Monetary Policy

Maurício Costa de Moura
Deputy-Governor for Institutional Relations, Citizenship and Conduct Supervision

Carolina de Assis Barros
Deputy-Governor for Administration

Otávio Ribeiro Damaso
Deputy-Governor for Regulation

Diogo Abry Guillen
Deputy-Governor for Economic Policy

Paulo Sérgio Neves de Souza
Deputy-Governor for Supervision

Fernanda Guardado
Deputy-Governor for International Affairs and Corporate Risk Management

Renato Dias de Brito Gomes (*)
Deputy-Governor for Licensing and Resolution

(*) Deputy Governor Renato Dias de Brito Gomes followed the first session of Comef, on March 1st, by videoconference, and did not participate in the second session, on March 2nd, as he attended an official meeting abroad.

Department Heads in charge of technical presentations:

André de Oliveira Amante – *Open Market Operations Department*
André Minella – *Research Department*
Edson Broxado de França Teixeira - *Deputy Governor for Supervision's Office*
Fabia Aparecida de Carvalho – *International Affairs Department*
Luis Gustavo Mansur Siqueira - *Financial Citizenship Promotion Department*
Gilneu Francisco Astolfi Vivan – *Financial System Monitoring Department*
Ricardo Franco Moura - *Prudential and Foreign Exchange Regulation Department*
Rogério Antonio Lucca - *Banking Operations and Payments System Department*

Other Participants:

Adalberto Felinto da Cruz Júnior – *Head of the Strategic Management and Specialized Supervision Department*
André Luiz Caccavo Miguel – *Deputy Head of the Financial System Monitoring Department*
Arnildo da Silva Corrêa – *Head of the Office of Economic Advisory*
Belline Santana – *Head of the Banking Supervision Department*
Climério Leite Pereira – *Head of the Resolution and Sanctioning Action Department*
Daniel Palaro Canhete – *Deputy Head of Department of Competition and Financial Market Structure*
Daniela Torres de Mesquita de S. Valle - *Head of the Governor's Office, substitute*
Eduardo José Araújo Lima – *Head of the Economic Policy Deputy-Governor's Office*
Enrico Bezerra Ximenes de Vasconcelos – *Head of the Secretariat of Governance, Coordination and Strategic Monitoring*
Erasto Villa Verde de Carvalho Filho – *General Counsel, substitute*

Eugênio Paccelli Ribeiro - *Executive-Secretary, substitute*
Fernando Alberto G Sampaio de Cavalcante Rocha – *Head of the Department of Statistics*
Harold Paquete Espínola Filho – *Head of the Credit Unions and Non-banking Financial Institutions Supervision Department*
Isabela Ribeiro Damaso Maia – *Head of the Sustainability and International Portfolio Investors Unit*
João André Calvino Marques Pereira – *Head of the Financial System Regulation Department*
Juliana Mozachi Sandri - *Head of the Conduct Supervision Department*
Luís Guilherme Siciliano Pontes – *Head of the Department of Foreign Reserves*
Mauro Zanatta – *Press Officer*
Olavo Lins Romano Pereira – *Deputy Head of the International Affairs Department*
Ricardo Eyer Harris – *Head of the Regulation Deputy Governor's Office*
Ricardo Sabbadini – *Head of the Department of Economics*
Ricardo Teixeira Leite Mourão –*Head of Deputy Governor for Licensing and Resolution's Office*
Sérgio Mikio Oyama – *Deputy Head of the Research Department*

The members of the Comef analyzed the recent evolution and prospects for financial stability in Brazil and in the international economies bearing in mind the objective of ensuring a sound, efficient, and competitive financial system. This document represents Comef's best effort to provide an English version of its meeting minutes. In case of inconsistency, the version in Portuguese language prevails.

A) Global financial markets

1. **The financial system of the main economies remains resilient.** Banking financial institutions in these countries hold robust levels of capital and liquidity. Simulations by the Central Bank of Brazil (BCB) and stress tests by jurisdictions indicate that the global financial system remains prepared to withstand additional shocks.

2. **Global financial conditions have eased since the last Comef meeting, despite some reversal in February.** The global disinflation process remains challenging and recent activity data consolidate the scenario of more prolonged global monetary tightening.

3. **Global Systemically Important Banks (GSIBs) continue to build provisions.** Expectations of lower economic growth, high interest rates and the persistence of inflation at high levels have resulted in real income losses, putting pressure on households' capacity to pay their debts. In some jurisdictions, this issue gains more relevance due to the predominance of mortgages with adjustable interest rates, which in scenarios of rising interest rates reduces debtors' payment capacity, increasing the risk of crises in the real estate sector, with potential systemic impact. Nevertheless, no significant deterioration has yet been observed in banks' credit portfolios, and the central banks of systemically important economies reiterate that their financial institutions are prepared to withstand an eventual materialization of adverse scenarios. Given the scenario of persistent global financial risks and domestic economic uncertainties, several jurisdictions preemptively maintained or increased their countercyclical capital buffers.

4. **The possibility of more abrupt changes in the conduct of monetary policy increases the risk of extreme scenarios of financial asset repricing materializing.** As expectations of a drop in inflation in the central economies are unmet, uncertainty about prospective scenarios rise, accentuating volatility in markets and increasing the odds of stress events, with global implications. In general, emerging economies have, so far, shown resilience in withstanding the sharp tightening of financial conditions observed since the end of 2021, but the high levels of public indebtedness resulting from efforts to combat the economic effects of the Covid-19 pandemic are a vulnerability factor. Transparency, predictability, and credibility in the conduct of monetary, fiscal and macroprudential policies are essential to mitigate systemic risks.

B) The National Financial System (SFN)

5. **The growth of broad credit slowed down in the different modalities.** Regarding households, the deceleration was greater in higher risk operations, such as those linked to payment transactions. In relation to legal entities, credit decelerated marginally. The capital market reduced its pace of expansion, but it remains a relevant source of financing, mainly for large companies.

6. **Provisions remain adequate, above expected loss estimates.** The increase in provisions is consistent with the greater materialization of risk that arises from the growth of credit in riskier modalities, the increase in the household debt service ratio, the reduction in the payment capacity of micro and small enterprises, and specific cases in large companies. Risk materialization should remain at a high level in the medium term, but more restrictive origination criteria in recent loans have helped to slow down the growth of problem assets in credit to households.

7. **Capitalization and liquidity of the SFN were preserved above prudential requirement levels.** The system has maintained sufficient capital and liquid assets to absorb potential losses in stressed scenarios and to comply with current regulations. The Comef remains attentive to the dynamics of savings accounts redemptions and their effects on mortgage lending. The profitability of the SFN reduced, mainly due to the increase in provisions, and remains pressured by the reduction of credit margin, low growth in service revenues and growth in administrative expenses due to inflation.

8. A significant portion of the provisions made in the FIs' balance sheets in the last quarter of 2022 is due to a specific event related to a large company. These provisions account for a relevant portion of the reduction in the annual profitability of the SFN and have already absorbed most of the risk materialization. The Central Bank estimated the remaining potential impact and simulated a contagion scenario over the entire production and supply chain with a relevant dependence on the company. In this extreme scenario, the impact on the consolidated SFN is negligible and there would be no capital non-compliance in any financial institution.

9. Stress tests' results show that the system is resilient. In the evaluated macroeconomic stress scenarios, described in the Financial Stability Report, the system would not face material non-compliances. Since the last Comef meeting, increase in uncertainty has amplified the impact on the system. The most severe impact continues to be observed in the scenario of a breakdown of confidence in the fiscal policy. A sensitivity analysis showed that even if problem assets doubled in relation to their current levels, the system would not face material non-compliances.

C) Main points of attention

10. The risk appetite of the FIs in lending to households and smaller enterprises decreased but remains high. Although decelerating, the pace of growth remains high in riskier modalities, such as credit card operations and consumer credit, which require more attention in an environment of worsening of household indebtedness and debt service ratio. However, at the margin, greater prudence in the concession of new loans generates better quality credit in these modalities. Regarding smaller companies, there was a deceleration in the pace of credit growth, but no relevant change has been seen in the granting criteria. Comef considers that it is important that financial intermediaries continue to preserve the quality standards of loan originations taking into account, notably, the total exposure of their clients in the National Financial System.

11. Isolated events in large companies generated a deterioration in asset prices in the corporate bond market. As a result of these events, volatility, spreads and risk aversion increased. Effects were also observed on some lines of credit. Comef follows the evolution and development of the recent events and remains ready to act in case of dysfunctionality.

12. High inflationary persistence raises the prospect of a more prolonged monetary tightening in advanced economies. An eventual materialization of extreme global financial assets repricing scenarios due to monetary tightening and abrupt changes in the conduct of monetary policy in advanced economies could lead to a significant impact on emerging economies, which so far have been resilient, even though vulnerability factors remain. Comef deems that the SFN's exposure to exchange rate risk is low and the dependence on external funding is small.

13. The Committee is attentive to the recent developments in the domestic and international scenarios and remains prepared to act, by minimizing any exacerbated spillover on the prices of local assets. The Committee continues to understand that macroeconomic policies that increase the fiscal predictability, reduce risk premiums and asset volatility, contribute to financial stability and, consequently, improve the payment capacity of agents.

D) Macroprudential policy decision

14. The Comef judges that the neutral macroprudential policy remains adequate for the current moment, characterized by the absence of significant accumulation of financial risks. Considering Comef's expectations on credit growth, there is no need to adjust macroprudential policy in the short term.

15. **Asset prices and credit growth are not a concern in the medium term, although there are uncertainties to be monitored.** Credit growth decelerated in the various modalities, and, at the margin, operations in higher risk lines have been originated with better credit quality. However, household indebtedness and debt service ratio remain high, and companies' payment capacity has declined. Thus, a substantial frustration in the performance of economic activity can result in an increase in credit risk. The Committee remains attentive to the contribution of the capital market to the growth of broad credit and its potential consequences for the accumulation of risks and monitors the developments of recent events that affected risk premiums in this market. The Comef continues to recommend that FIs maintain prudence in credit and capital management policies.

16. **The Comef decided that, given the current conditions and the economic outlook, the Countercyclical Capital Buffer for credit exposures in Brazil will remain at 0% over the next meetings.** Rises in the buffer come into effect only one year after a decision by the Comef. The decision considered the restrictive financial conditions of the domestic and international environment, the asset prices, and the expectations regarding the evolution of the credit market.

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