BANCO CENTRAL DO BRASIL

Economic Policy Board

Investor Relations and Special Studies Department

External Accounts

with information up to February 2015

Frequently
Asked Questions
Series

External Accounts

This paper is part of the Banco Central do Brasil's "Frequently Asked Questions" series. This series, which is produced by the BCB's Investor Relations Group (Gerin), provides background information and analysis on economic data and issues of interest to investors and the general public. The Banco Central do Brasil is producing this series as part of its ongoing efforts to enhance the transparency of the Brazilian economic policy, and to improve its communication with the private sector.

Contents

External Accounts

1. How are Brazil's external accounts released?

Since January 2001, the Central Bank releases Brazilian external accounts according to the methodology recommended in "Balance of Payments Manual" (5th edition, 1993) issued by the International Monetary Fund (IMF). This manual defines international standards for the calculation of the external accounts in an integrated way, covering data flows (the Balance of Payments itself) and data on stocks of international financial assets and liabilities carried by the country.

From April 2015 onwards, Brazil's Central Bank will announce the external sector statistics of the Brazilian economy in accordance with the sixth edition of the IMF Balance of Payments Manual and International Investment Position (BPM6). However, all data related to Balance of Payments in this FAQ still use the 5th edition methodology, since the historical data series are not completed yet.

2. Which structure does the Balance of Payments follow?

The Balance of Payments (BoP) is structured in two large account groups:

- Current Account, which combines balance on goods, services balance, income account and net current unilateral transfers; and
- Capital and financial account, which combines foreign direct and portfolio investments in the country and of Brazilians abroad, in addition to derivatives operations and other investments.

The sum of the results of the current and capital and financial accounts is the BoP result, which, by definition, is equal to the change in international reserves under the international liquidity concept. Errors and omissions may give rise to a statistical discrepancy between the two flows, which is duly registered in the BoP.

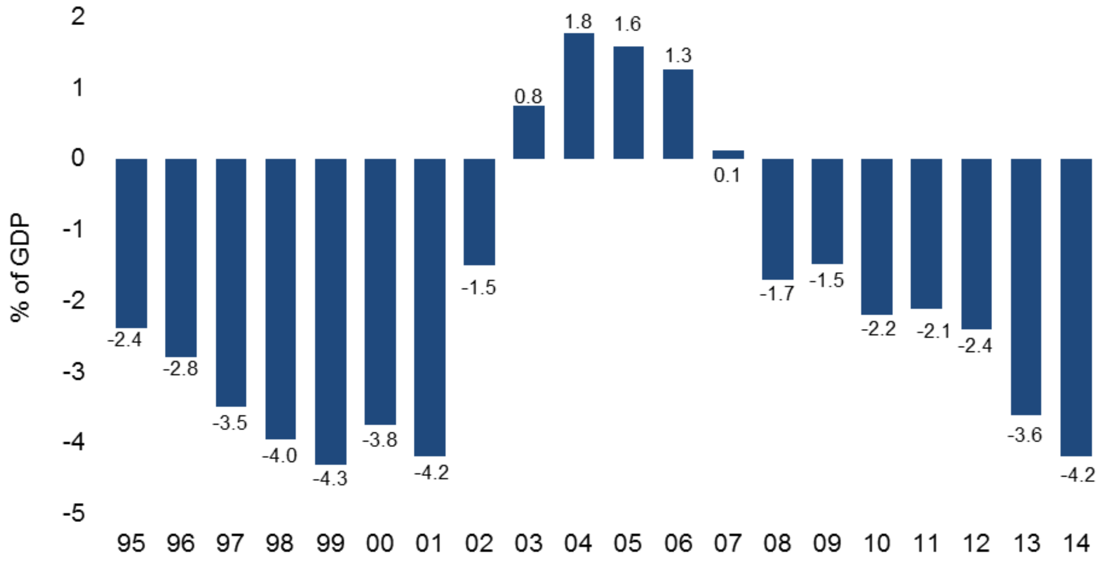
3. How has the current account balance evolved in recent years?

Brazil's current account balance has undergone two distinct phases since the implementation of the Real Plan in July 1994. As shown in Graph 1, until 1999, deficits were increasing, reaching a historical peak as a proportion of GDP[1] in that year (US$25.3 billion, equivalent to 4.32% of GDP). From this year on, however, with the adoption of the inflation targeting regime, which has as one of its pillars the floating exchange rate regime, there was gradual adjustment in the Brazilian current account. The balance had a surplus in 2003, influenced by the strong depreciation of the Brazilian currency in 2002, and remained positive until 2007. From 2008 on, with the intensification of the international crisis and the consequent decline in global growth, our external accounts returned to present current account deficit.

[1] Foreign Sector Press Release, T. 1 or SGS 11728 (all references to 'SGS' regard codes of search at: https://www3.bcb.gov.br/sgspub/localizarseries/localizarSeries.do?method=prepararTelaLocalizarSeries)

Graph 1

Current Account Balance



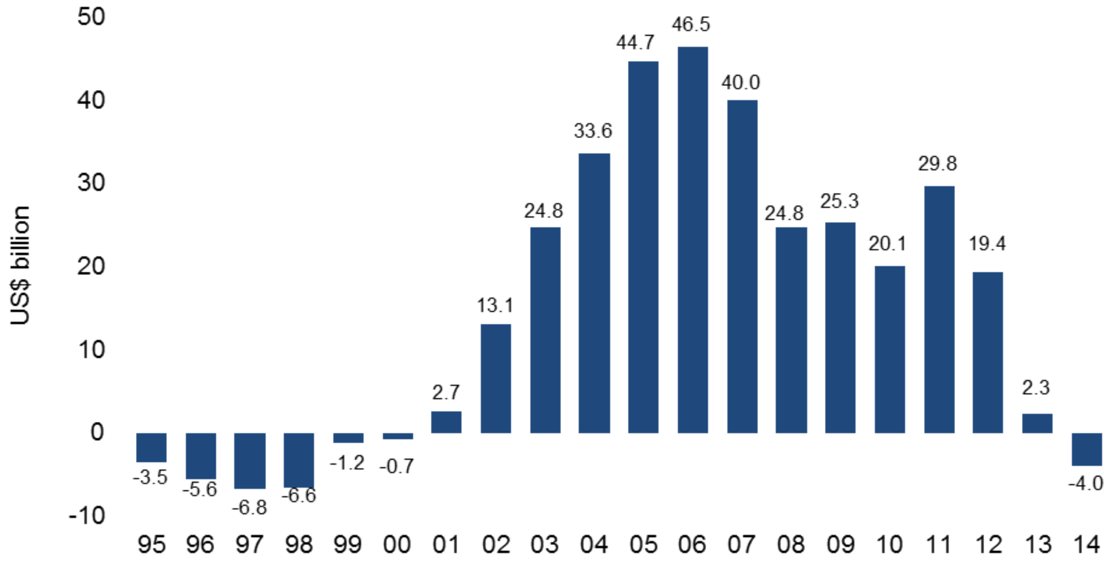
Source: BCB

4. How has the trade balance evolved in recent years?

The decrease in the current account deficit[2] after 1999 is basically due to the improvement in the trade balance. As shown in Graph 2, the increase in the Brazilian trade balance from 1998 to 2006 totaled US$53 billion, an amount higher than the current account balance change in the same period (US$47 billion). Note that in 2006 the trade balance registered a US$46.5 billion surplus, a historical record.

Graph 2

Trade Balance



Source: MDIC

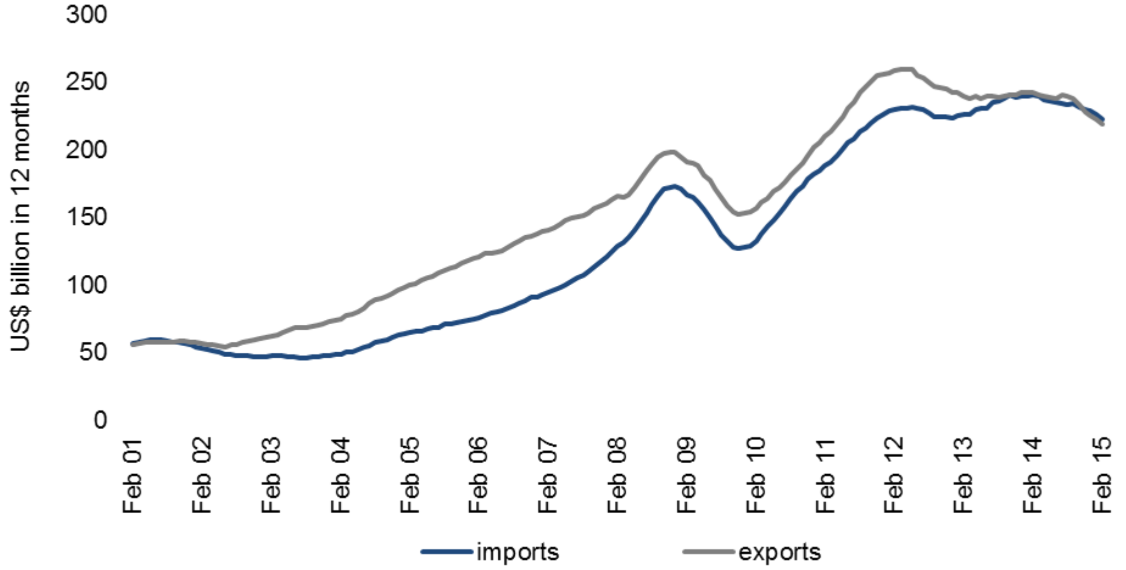
[2] Foreign Sector Press Release, T. 1 or SGS 2302

The significant improvement in the trade balance was driven by the increase in exports[3] since the second half of 2002 up to November 2008, when a historical peak of US$198.4 billion accumulated in 12 months was reached for exports, subsequently surpassed from December 2010 on. The better exports performance enabled the country to increase significantly its imports, hampering at the same time the deterioration of the external accounts results. In the period shown in Graph 3, the amount of imports[4] accumulated in 12 months rose from the minimum of US$46 billion in August 2003, to a maximum of US$173.1 billion in December 2008. Although the international crisis impacted for a period this development, the upwards trend resumed in December 2009, with a continuous growth in the 12-month accumulated imports, and successive records since October 2010, reaching US$241.1 billion in February 2014 (US$222.7 billion in February 2015). There are several factors affecting the performance of the trade balance, such as the level of domestic economic activity, external demand, tariffs and trade barriers. The higher demand from the rest of the world as compared to Brazil, and a favorable real effective exchange rate explain the acceleration of exports growth from 2002 to 2005. Since then, besides exports, imports also started to grow more rapidly, reflecting a higher relative growth of domestic demand, as compared to the rest of the world. As a consequence of the substantial increase of both exports and imports, Brazilian total external trade presented successive records up to 2008. In 2009, with lower activity worldwide due to the intensification of the international financial crisis after the Lehman Brothers bankruptcy, the Brazilian external trade decreased, and both exports and imports fell substantially, recovering after 2010. Total trade reached US$491 billion in May 2012, and US$441.7 billion in February 2015.

Graph 3

Exports and Imports

(up to Feb/15)



Source: MDIC

[3] Foreign Sector Press Release, T. 1 or SGS 2733
[4] Foreign Sector Press Release, T. 1 or SGS 2734

5. What is the real effective exchange rate?

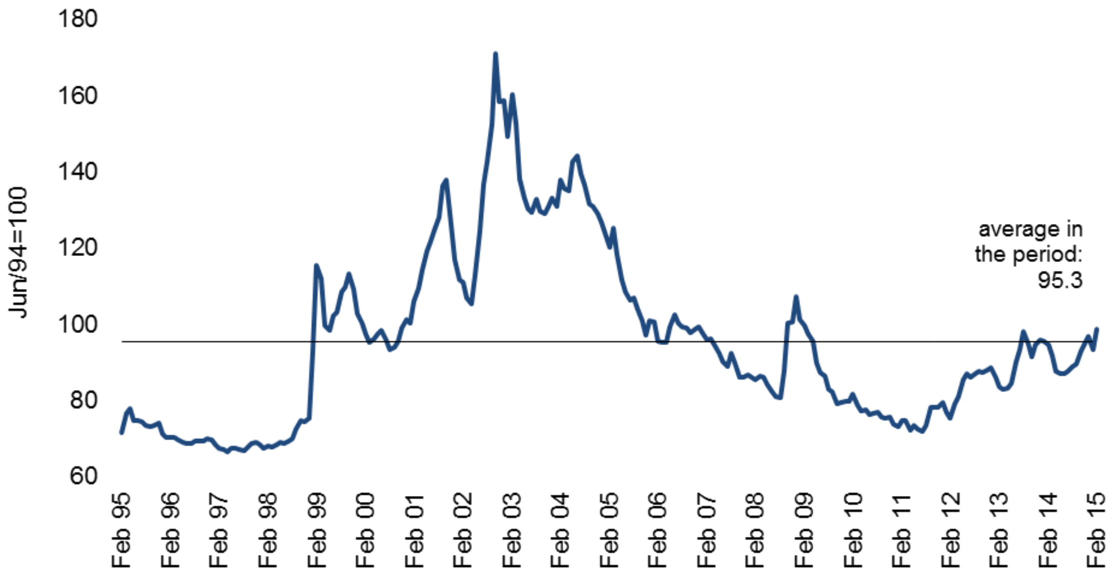
The real effective exchange rate (REER)[5] is a measure of export competitiveness. It is the average exchange rate of the Brazilian *real* against the currencies of our 15 main trade partners, weighted by the share of these countries in the total Brazilian exports. A domestic inflation index is used as an internal deflator, and the CPIs of each trade partner serve as external deflators. Thus, it is a broader indicator than bilateral exchange rates to indicate exports competitiveness.

As shown in Graph 4, after the introduction of the Brazilian new currency in 1994, the *real*, the REER, deflated by IPCA, appreciated up to January 1999, when the *real* depreciated and floating exchange rate regime was implemented. Since then, the REER depreciated significantly through the second half of 2002, when a new cycle of appreciation started. The graph shows that, in mid-2008, in the recent international financial crisis apex, exchange rate depreciated again, but for a short time, appreciating from the beginning of 2009 up to mid-2011. Compared to the average in February 1995-February 2015, the most recent REER (Feb/15) stands slightly above the historical average for the period.

Graph 4

Real Effective Exchange Rate

(up to Feb/15)



Source: BCB

6. How has the balance of services evolved in Brazil?

The services account[6] has been deteriorating in recent years, contributing for the recent decrease in the current account balance. Table 1 shows the services account broken down by its main components in the last six years. The downward trajectory of international travel income[7] may be explained by an environment with higher available

[5] http://www.bcb.gov.br/?INDECO, T. 5.28 or SGS 11752
[6] Foreign Sector Press Release, T. 1 or SGS 2305
[7] Foreign Sector Press Release, T. 5 or SGS 2313

income and nominal appreciation of the exchange rate, observed up to the last quarter of 2008, when the international financial crisis deepened, and after the crisis, with the recovery. Higher imports and more Brazilians traveling abroad impacted expenses with freights and tickets, increasing net transportation costs[8].

The main component of services account, operational leasing account[9], also registered a sharp deficit increase during the crisis deepening, and kept an upward trend, mainly due to the rent of equipment related to oil exploration.

Table 1

Services Balance

(US$ million)

	2009	2010	2011	2012	2013	2014
Services	-19,245	-30,835	-37,932	-41,042	-47,101	-48,928
Transportation	-3,926	-6,407	-8,335	-8,770	-9,793	-8,939
Travel	-5,594	-10,718	-14,709	-15,588	-18,283	-18,695
Computer and Information	-2,586	-3,296	-3,800	-3,850	-4,469	-4,427
Operational Leasing	-9,393	-13,752	-16,686	-18,741	-19,060	-22,651
Other	2,253	3,337	5,598	5,907	4,503	5,784

Source: BCB

7. What is the Brazilian income account and how has it been evolving?

The income account[10] registers compensations of employees and investment incomes[11], which correspond to the remuneration of funds detailed in the financial account, as shown in Table 2. Direct investment incomes[12] encompass profits and dividends relative to equity ownership and interest corresponding to intercompany direct loans or with securities of any maturity. They do not include capital gains, registered as direct investment in the financial account. Portfolio investment incomes[13] comprise profits, dividends and bonuses relative to stocks ownership and interests corresponding to ownership of domestically issued debt securities (domestic public debt securities, debentures and other private securities) and securities issued abroad (bonds, notes and commercial papers) of any maturity. Exceptions are interests relative to the placement of securities between linked corporations, registered as direct investment income. Other investments incomes[14] register interest on trade credits, such as suppliers' credits; interest on loans from governmental agencies, international organisms, banks and buyers; and the relative to interests on deposits and other assets and liabilities.

The income account has historical deficit in Brazil. However, one may note a recent change in its pattern, when net remittances of direct investment incomes – profits and dividends, became the main item in the income account, overcoming since 2007 remittances of interest and portfolio investment income. This is due to the economic development that allowed an increase in the FDI inflow and the rate of return of this capital, increasing the remittances of profits and dividends.

[8] Foreign Sector Press Release, T. 5 or SGS 2306
[9] Foreign Sector Press Release, T. 5 or SGS 2343
[10] Foreign Sector Press Release, T. 6 or SGS 2385
[11] Foreign Sector Press Release, T. 6 or SGS 8031
[12] Foreign Sector Press Release, T. 6 or SGS 7946
[13] Foreign Sector Press Release, T. 6 or SGS 7951
[14] Foreign Sector Press Release, T. 6 or http://www.bcb.gov.br/?BALANCESPECIAL

Table 2

Income Account

(US$ million)

	2009	2010	2011	2012	2013	2014
Incomes	-33,684	-39,486	-47,319	-35,448	-39,778	-40,323
Compensation of Employees	603	498	567	511	511	354
Investment Income	-34,287	-39,985	-47,886	-35,959	-40,289	-40,677
Direct Investment Income	-19,742	-25,504	-29,631	-19,960	-22,547	-23,476
Portfolio Investment Income	-9,213	-9,964	-12,164	-9,911	-11,003	-11,102
Other Investments Income	-5,332	-4,517	-6,091	-6,088	-6,738	-6,100

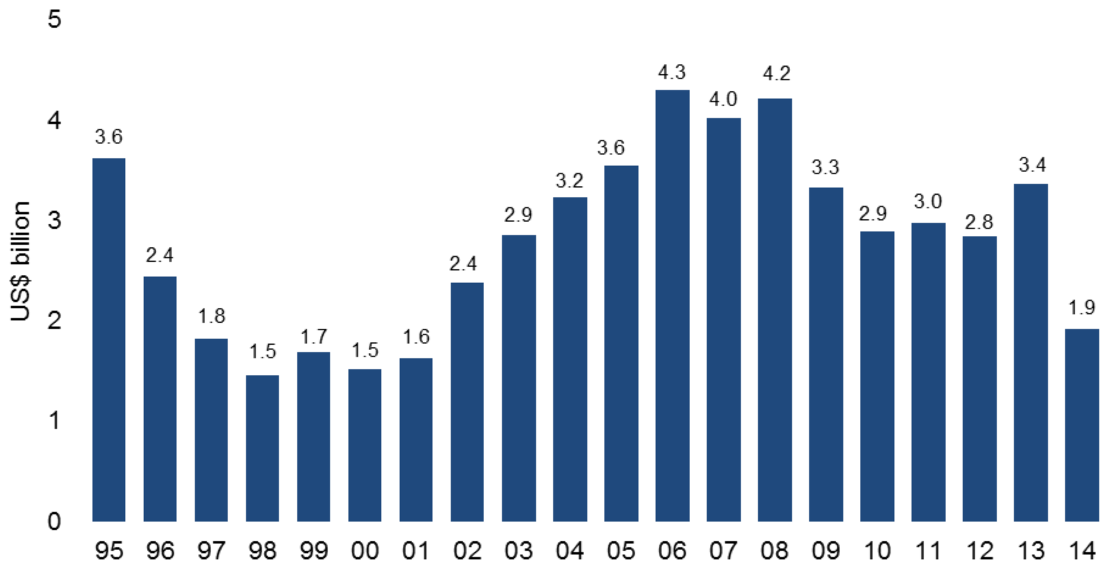
Source: BCB

8. What are and how have the current unilateral transfers been evolving in Brazil?

The current unilateral transfers[15] comprehend payments and receipts, as goods and currency, for current consumption, which do not correspond to a purchase or sale. Transfers relative to assets of international migrants, registered in the capital account, are excluded. Graph 5 shows the evolution of unilateral transfers since 1995.

Graph 5

Current Unilateral Transfers



Source: BCB

9. What is and how has been evolving the foreign direct investment (FDI) in Brazil?

Foreign Direct Investment (FDI)[16] comprises direct investment abroad and direct investment in Brazil. Both accounts comprise equities and intercompany loans. Investment abroad registers external assets owned by residents in Brazil as direct investment, while investment in Brazil comprehends investment made by foreigners in Brazil. This kind of investment has a longer-term profile.

[15] Foreign Sector Press Release, T. 1 or SGS 2410

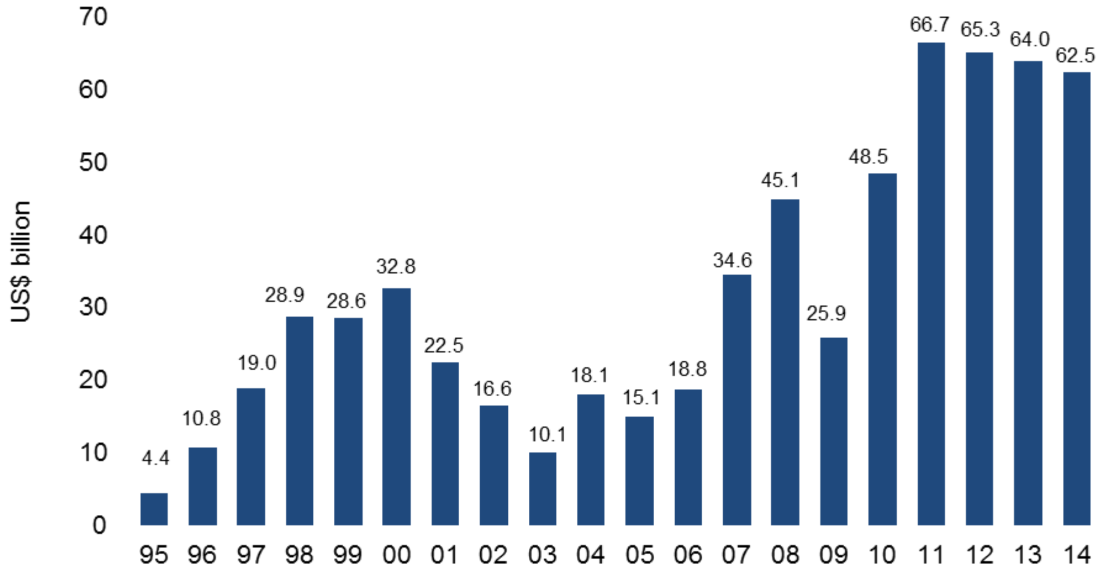
[16] Foreign Sector Press Release, T. 1 or SGS 2430

With the implementation of Real Plan in 1994, direct investment in Brazil assumed an upward trend up to 2000, with foreign companies attracted by the stability scenario, growing domestic demand and privatizations (Graph 6). 2001 and 2002 revealed FDI flows decreasing worldwide and, along with uncertainties associated to presidential elections in Brazil in 2002, particularly in sectors with redefinition of the regulatory environment, contributed to reducing the balance from 2001 to 2003. Since 2004 there has been a resumption of the trend of growing FDI inflows, with industry as the main attractive segment. Even with the crisis that affected financial markets from the second half of 2007 on, and its impacts in the real sector of the main developed economies, FDI reached a record of net US$45.1 billion in 2008, most of it (approximately 40%) headed to the services sector, mainly financial services and auxiliary activities.

From the second half of 2008 on, FDI balances to Brazil decreased, as expected in a crisis scenario, where, due to financial losses, countries tend to reduce their investment abroad. After recovering in 2010, FDI reached a new record in 2011 (US$66.7 billion), assuming a downward trend since then.

Graph 6

Net FDI



Source: BCB

10. What are external financing needs?

External financing needs comprehend the current account deficit[17] deducted by the net FDI (including intercompany loans), i.e., corresponds to the parcel of the current account deficit that is not financed by the net inflow of direct investment. When the net inflow of FDI is more than enough to finance the current account deficit, needs are negative. The higher the long-term international capital flows to Brazil, the lower the external fragility degree of the Brazilian economy.

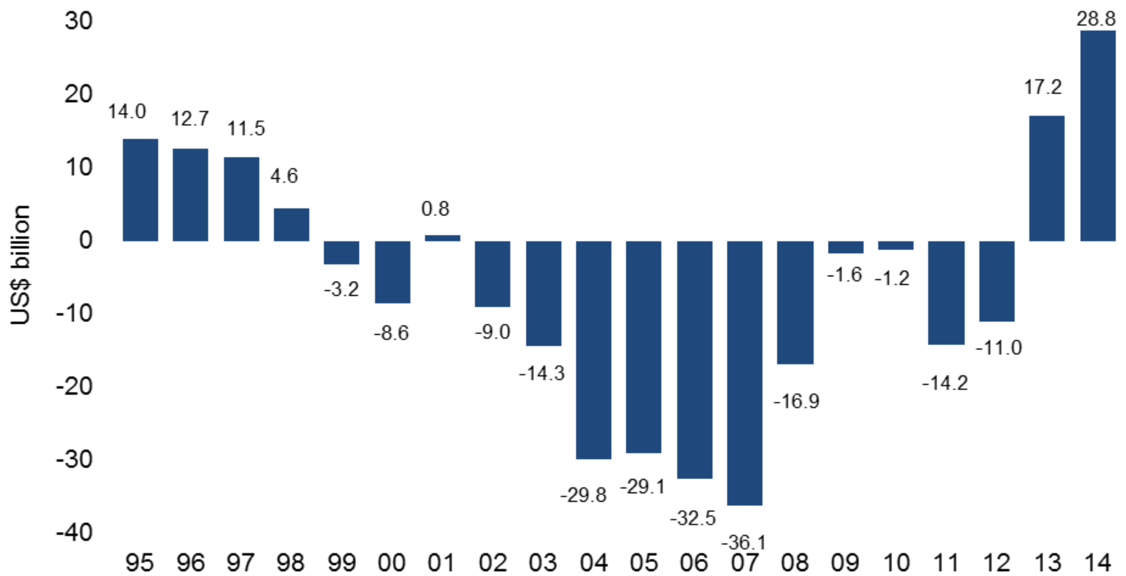
Graph 7 shows a recent evolution of the Brazilian external financing needs. Since 1995, the Brazilian external sector had the tendency to strengthen. In 2008, however,

[17] Foreign Sector Press Release, T. 1 or SGS 2301

the downward trajectory for the external financing needs started to reverse, in spite of a growing FDI, due to the current account balance, the worst since 1998. In 2009, FDI decreased sharply and there was a sizable current account deficit, increasing external financing needs to the worst result since 2001. These were visible effects of the 2008 international crisis on the Brazilian economy, which recovered in 2011, when external financing needs were negative at around US$14.2 billion. In 2014, the external financing needs resumed growth, reaching US$28.8 billion, a result of the deepening of the current account deficit.

Graph 7

External Financing Needs



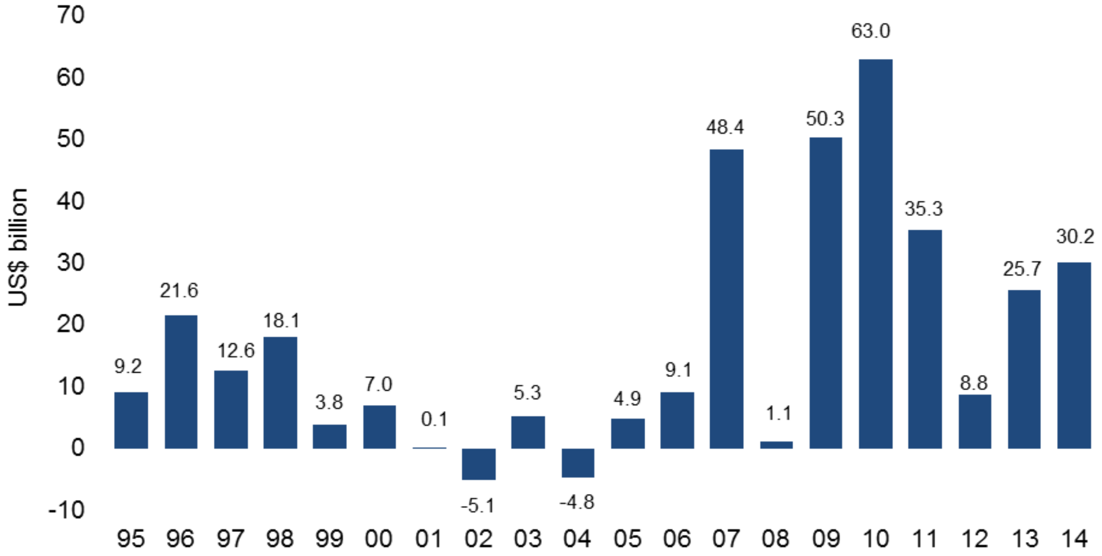
Source: BCB

11. How has portfolio investment been evolving in Brazil?

Portfolio investment registers flows of assets and liabilities comprised of issuance of credit securities commonly negotiated in the secondary market. Asset-side of portfolio investment refers to Brazilian funds used to purchase foreign securities, negotiated domestically or abroad. Liabilities-side registers purchases by non-residents of equities and fixed rate securities issued in Brazil. Graph 8 shows the evolution of the net portfolio investment[18] since 1995.

[18] Foreign Sector Press Release, T. 1 or SGS 2442

Graph 8
Portfolio Investment



Source: BCB

In 2007, portfolio investment increased significantly, reaching a historical record, US$48.4 billion. This result was a consequence of the improvement in the Brazilian external accounts, a higher credibility in the market and the declining trajectory of country-risk, and Brazil attracted many investors not only in equities, with investments summing US$26.2 billion, but also in fixed rate securities, which totaled US$21.9 billion in 2007.

Due to the international financial crisis, which reached its apex in the second half of 2008, and a higher risk aversion, investors withdrew their resources from emerging markets, reallocating them in more liquid and less risky assets, reducing portfolio investment balance to US$1.1 billion in 2008. In 2009, with a relative improvement in the world economic scenario and a reduction in the stress of financial markets, investors started again to buy assets in Brazil, due to better opportunities of gains in the country, with the historical peak reached in 2010 (US$63 billion), and decreasing in the two following years, resuming an upward trend thereafter.

12. What are the Uses and Sources of the Balance of Payments?

The Uses and Sources of the BoP[19] is an alternative presentation of the external accounts, including every item of BoP reorganized, such as to illustrate how FX resources are supplied (Sources) to meet the demands for FX from current transactions and payments of external credits (Uses). Table 3 shows annual Uses and Sources from 2009 to 2014.

[19] http://www.bcb.gov.br/?BALANCESPECIAL

Table 3

Uses and Sources – 2009 to 2014

(US$ million)

	2009	2010	2011	2012	2013	2014
Uses	**-54,423**	**-81,117**	**-90,173**	**-93,922**	**-141,297**	**-142,062**
Current account	-24,302	-47,273	-52,473	-54,249	-81,227	-91,288
Trade balance	25,290	20,147	29,793	19,395	2,286	-3,959
Services and income	-52,930	-70,322	-85,251	-76,489	-86,879	-89,251
Interests	-9,069	-9,610	-9,719	-11,847	-14,244	-14,154
Profits and dividends	-25,218	-30,375	-38,166	-24,112	-26,045	-26,523
Travel	-5,594	-10,718	-14,709	-15,588	-18,283	-18,695
Other	-13,049	-19,619	-22,656	-24,942	-28,308	-29,879
Current unilateral transfers	3,338	2,902	2,984	2,846	3,366	1,922
Medium- and long-term ammortizations	-30,121	-33,844	-37,700	-39,673	-60,070	-50,774
Bonds, notes and commercial papers	-13,028	-15,735	-9,515	-11,395	-15,518	-14,819
Trade credits	-3,787	-2,601	-2,754	-1,710	-1,493	-1,716
Loans	-13,307	-15,508	-25,430	-26,568	-43,060	-34,239
Sources	**54,423**	**81,117**	**90,173**	**93,922**	**141,297**	**142,062**
Capital account	1,129	1,119	1,573	-1,877	1,193	590
Foreign direct investment	25,949	48,506	66,660	65,272	63,996	62,495
Equities and long-term debt securities issued in the country	47,148	52,272	7,114	10,651	37,006	31,652
Medium- and long-term disbursements	35,830	62,598	83,586	57,813	60,819	72,226
Bonds, notes and commercial papers	12,606	25,847	27,108	17,403	13,176	16,242
Trade credits	2,742	2,066	1,589	1,252	2,768	2,961
Loans	20,482	34,684	54,889	39,158	44,875	53,023
Brazilian investments abroad	-15,845	-58,805	-20,866	-29,343	-44,971	-39,435
Short-term and other	6,864	24,529	10,743	10,306	17,328	25,367
Reserve assets	-46,651	-49,101	-58,637	-18,900	5,926	-10,833

Source: BCB

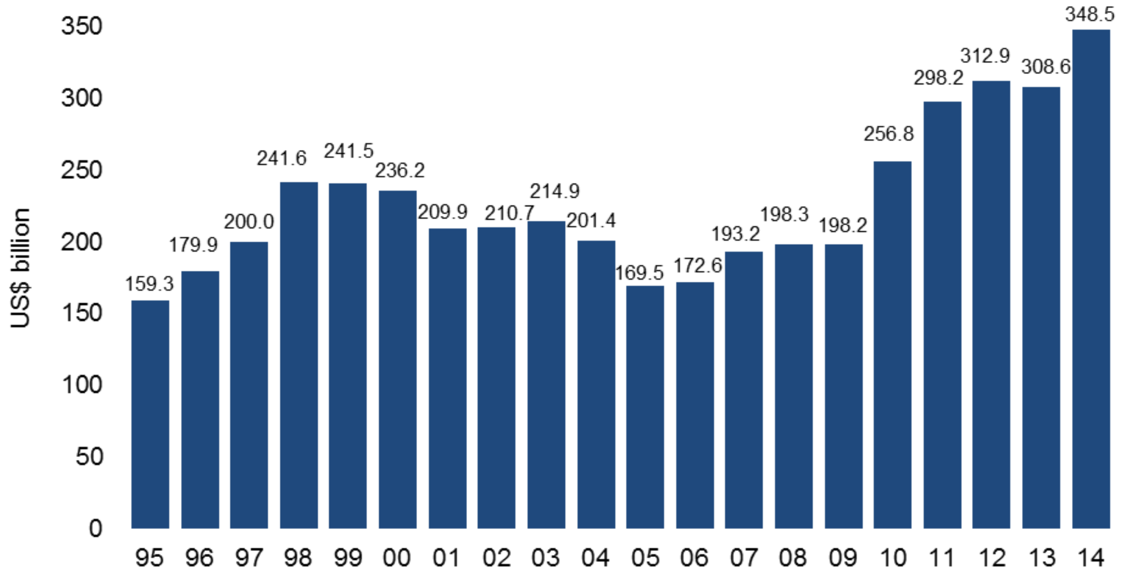
13. How big is the total external debt? What is its recent evolution?

Graph 9 shows the historic of total Brazilian external debt[20] since 1995. The 90s brought an accelerated increase of external debt, reaching a record in 1998, summing US$241.6 billion. Since then, external debt fell slightly up to 2003 and sharply in 2005, reaching US$169.5 billion. After then, it increased up to 2007 and kept relatively stable until 2009, surpassing US$300 since 2012.

[20] Foreign Sector Press Release, T. 59 or SGS 3682

Graph 9

Total External Debt



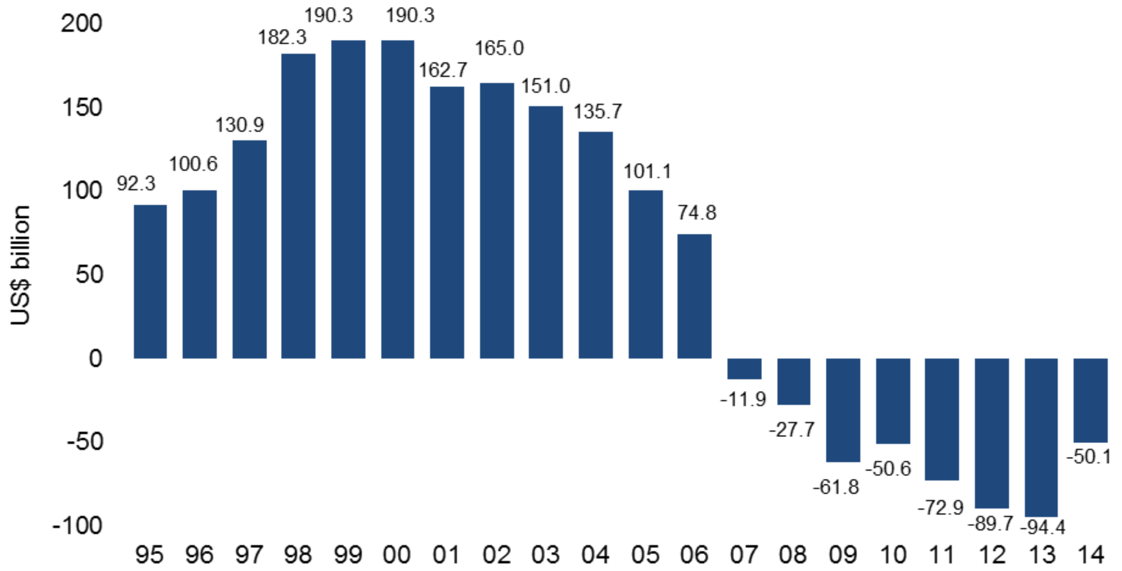
Source: BCB

14. How big is the net external debt?

Net external debt[21], which is the total external debt deducted by international reserves, commercial banks assets abroad end Brazilian credits abroad, became negative in 2007 (Graph 10). Thus, Brazil became an international net creditor, since its registered total external debt became lower than its foreign exchange reserves.

Graph 10

Net External Debt



Source: BCB

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[21] Foreign Sector Press Release, T. 59 or SGS 3683

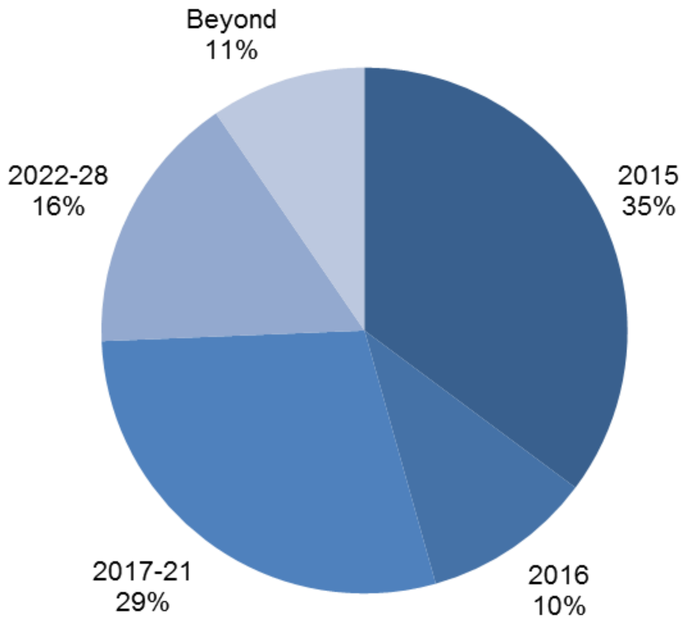
15. What is the maturity profile of the Brazilian external debt?

Most of the Brazilian registered external debt matures in the long-term[22], even after the recent international financial crisis, when short-term debt increased substantially. Graph 11 shows that, in December 2014, 74% of pending debt matures up to 2021 and just only 35% will mature in 2015. On the other hand, 11% of total debt matures after 2029.

Graph 11

Registered External Debt – Maturity

(Dec/14)



Source: BCB

16. How is the debt broken down by currency?

In December 2014, most of the registered external debt was denominated in US dollars (90.6%), whilst Brazilian *real* responded for 3.3% of that total, the same share of the euro (Graph 12). There is still 1.0% of the debt in yens, 1.2% in SDR (Special Drawing Right), the IMF "currency", and small denominations of the debt in Swiss francs, Sterling pounds, Canadian dollars and other, which sum 0.2% of the total[23].

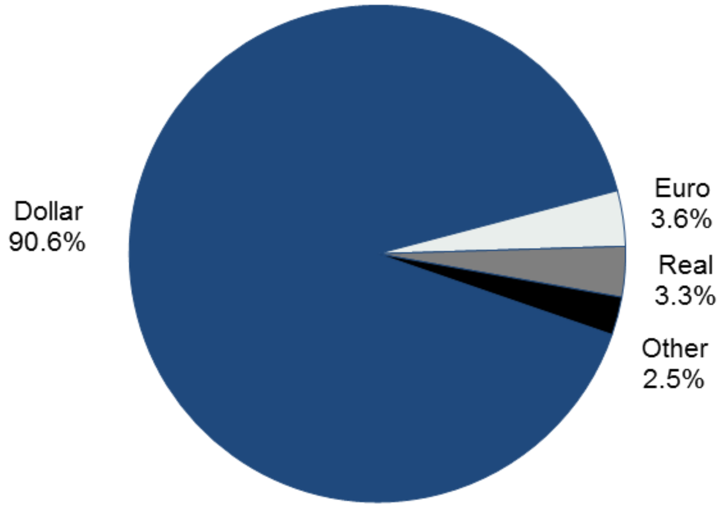
[22] Foreign Sector Press Release, T. 53 e 53-A

[23] Foreign Sector Press Release, T. 55

Graph 12

Registered External Debt – By Currency

(Dec/14)



Source: BCB

17. What share of the external debt is fixed interest rate?

In December 2014, 50.5% of the registered external debt was taken at fixed interest rates and 49.5% at floating rates, 44.9% of which was linked to Libor[24].

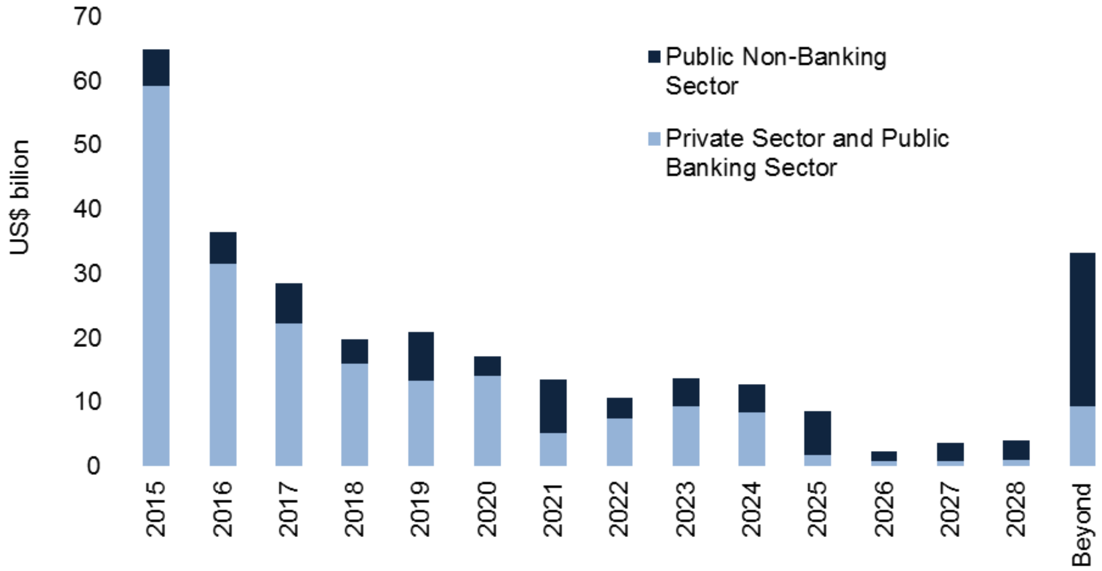
18. What proportion of the external debt is owed by the public sector and what is the schedule for amortizing principal?

In December 2014, non-banking public sector (including National Treasury, Central Bank, state and municipal governments and state-owned companies) was responsible for 30.9% of total registered external debt, totaling US$89.8 billion. Private sector and banking public sector responded for the remaining 69.1%, totaling US$201.1 billion[25]. Regarding the schedule of the amortization for the principal external debt[26], medium- and long-term profile predominates in the debt of non-banking public sector, as shown by Graph 13. Out of the US$65.0 billion maturing in 2015, only 8.9% is from non-banking public sector, while for debt maturing in 2028 and beyond, which totaled US$37.4 billion, this percentage reached 72.2%.

[24] Foreign Sector Press Release, T. 56
[25] Foreign Sector Press Release, T. L52
[26] Foreign Sector Press Release, T. 54 e 54-A

Graph 13

Registered External Debt - Principal Amortization Schedule



Source: BCB

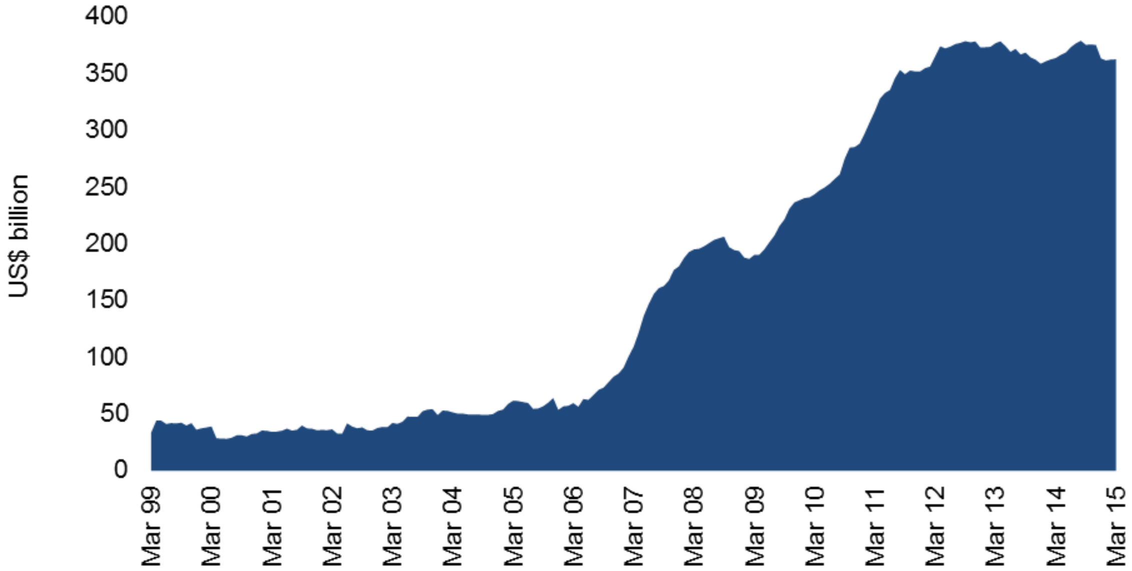
19. How is the evolution of international reserves?

In 2004, with an improved external scenario, a process of accumulation of international reserves through purchases of dollars in the spot market was implemented by the Central Bank. Since then, international reserves[27] have been reaching record levels, becoming one of the main reasons for the stronger external sustainability of the Brazilian economy, together with the reduction of the public external debt. This better Brazilian external position, which contributes for the lower sensitiveness of our economy to external shocks, was one of the fundamental factors for the achievement of the investment grade granted by rating agencies in recognition of the higher safety of Brazil as destiny for foreign investment.

In 2008, with the deepening of the international financial crisis, the Central Bank had to temporarily stop the process of foreign exchange reserves accumulation. This resulted in a slight reduction of international reserves from the end of 2008 to the beginning of 2009, as shown in Graph 14. From mid-2009, with less stress in the international financial market, the net supply of currency in the foreign exchange domestic market resumed, which led the Central Bank to restart the accumulation reserves.

[27] Foreign Sector Press Release, T. 49 or SGS 3546

Graph 14
International Reserves
(up to Mar/15)

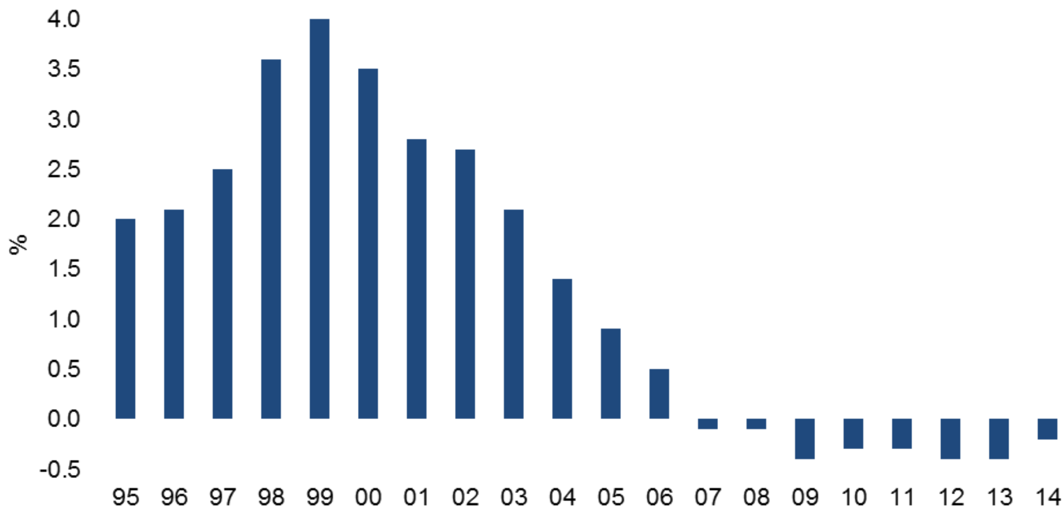


Source: BCB

20. How have some external sustainability indicators in Brazil been evolving?

The international financial crisis served as a test to the government strategy of accumulating international reserves since 2004. The relatively modest impact of the crisis over Brazilian external accounts showed that, indeed, our economy is more solid than before. International reserves served as a kind of insurance, improving the perception of the market regarding stability and sustainability of Brazilian economy. Graphs 15 to 17 show the evolution of some of the main Brazilian indicators of external sustainability.

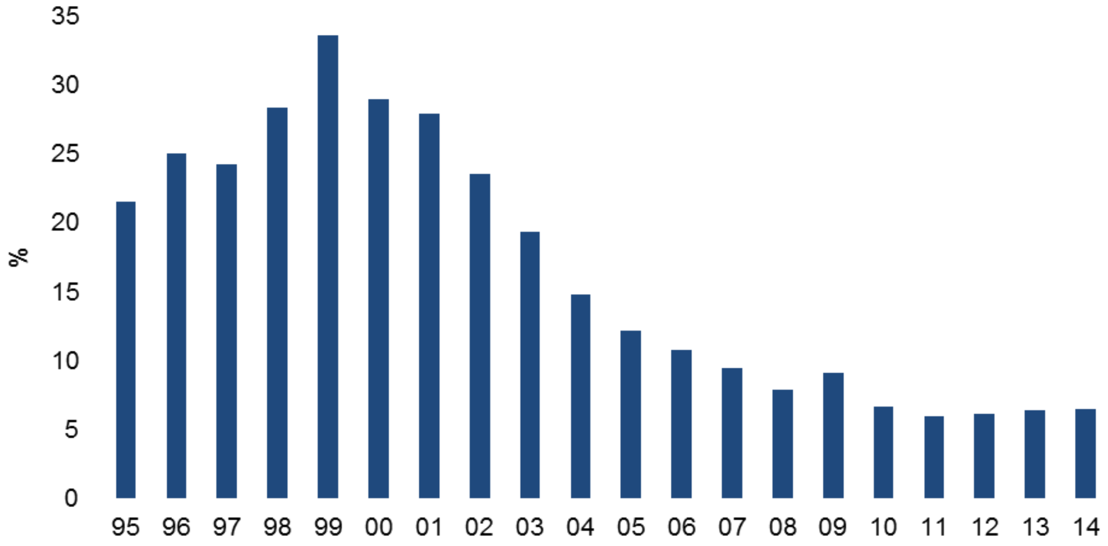
Graph 15
Net External Debt/Exports



Source: BCB

Graph 16

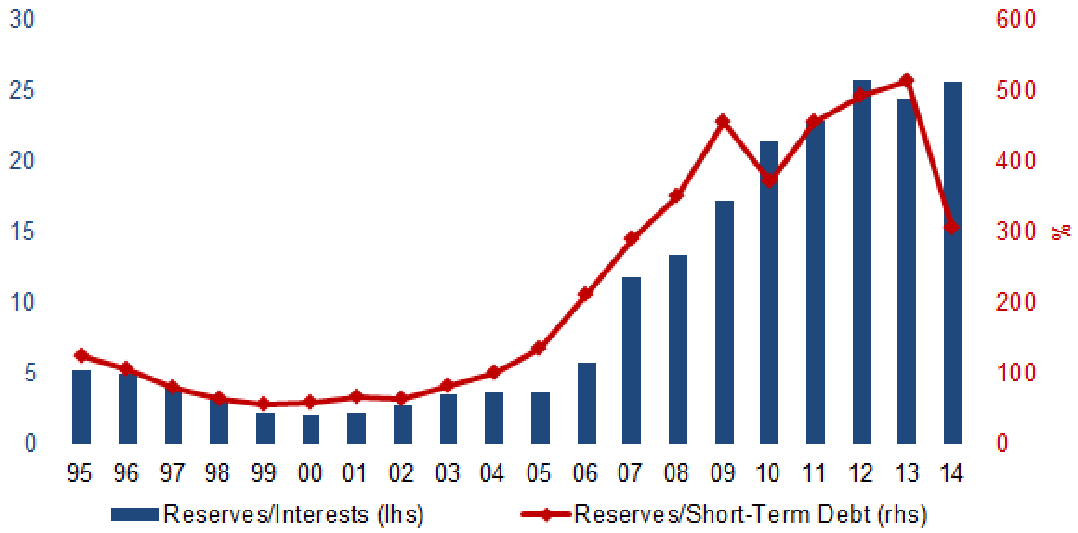
Interests/Exports



Source: BCB

Graph 17

Reserves/Short-Term Debt and Reserves/Interests*



*includes amortization of medium- and long-term debt due in the next 360 days. Source: BCB

21. Where can I get more information and updated data about the Brazilian BoP?

The Central Bank releases a monthly "Foreign Sector Press Release", with tables detailing the BoP accounts, international reserves and external debt, including the update schedule of amortization and interest payments. The "Foreign Sector Press Release" is available at http://www.bcb.gov.br/?FOREIGNSECTOR.

Data historical series related to the tables and graphs presented in this text may be checked at the Central Bank webpage (http://www.bcb.gov.br/?TIMESERIESEN and https://www3.bcb.gov.br/sgspub/localizarseries/localizarSeries.do?method=prepararTel aLocalizarSeries), selecting by subject ⇒ External sector, or by code, using the codes informed in the notes, and tables from the Press Release.

BoP special series may be checked at http://www.bcb.gov.br/?BALANCESPECIAL.

The Central Bank also releases Excel worksheets with the main economic indicators at http://www.bcb.gov.br/?INDICATORS. BoP indicators are in Chapter V.

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Central Bank of Brazil

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