JP Morgan Investor Seminar
Washington, USA

April 21st, 2017

Brazil: Economic and Monetary Outlook

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and Corporate Risk Management

1. **International Context and External Sector**

2. Growth Dynamics: stabilization and signals of recovery

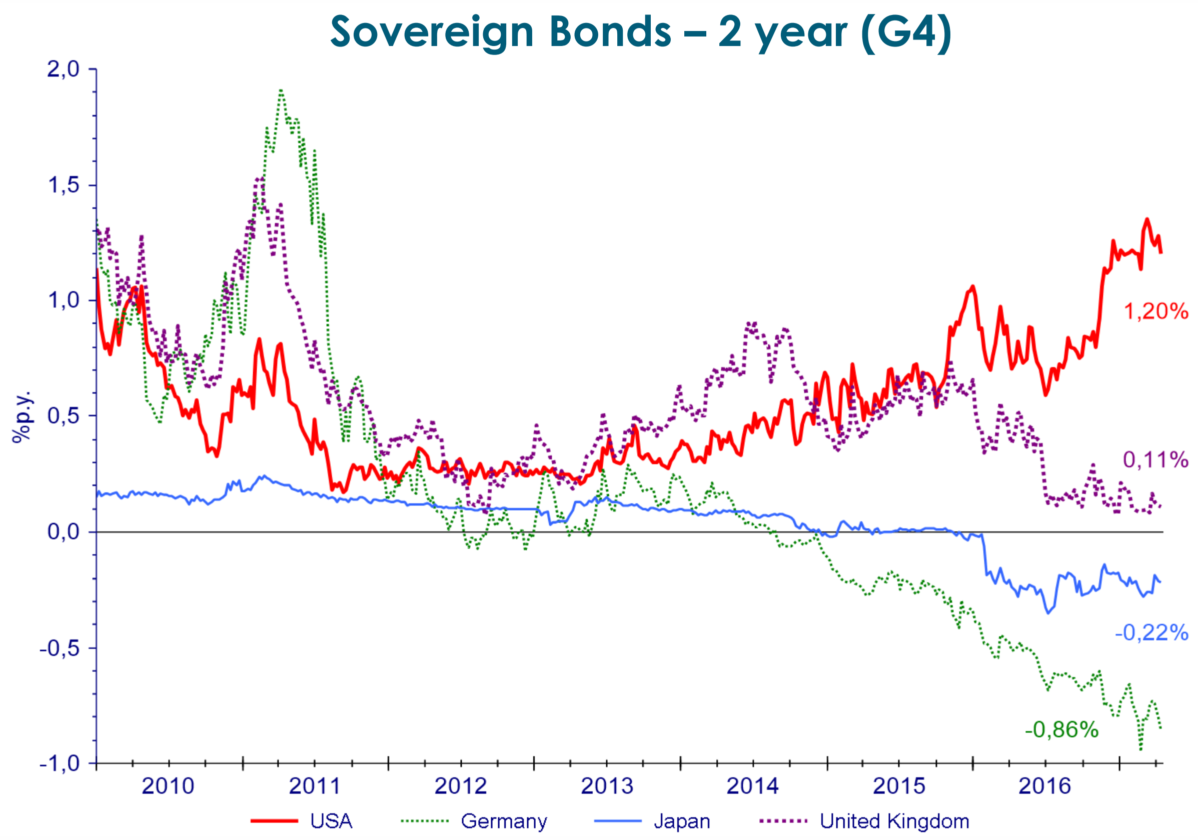
3. Monetary Policy

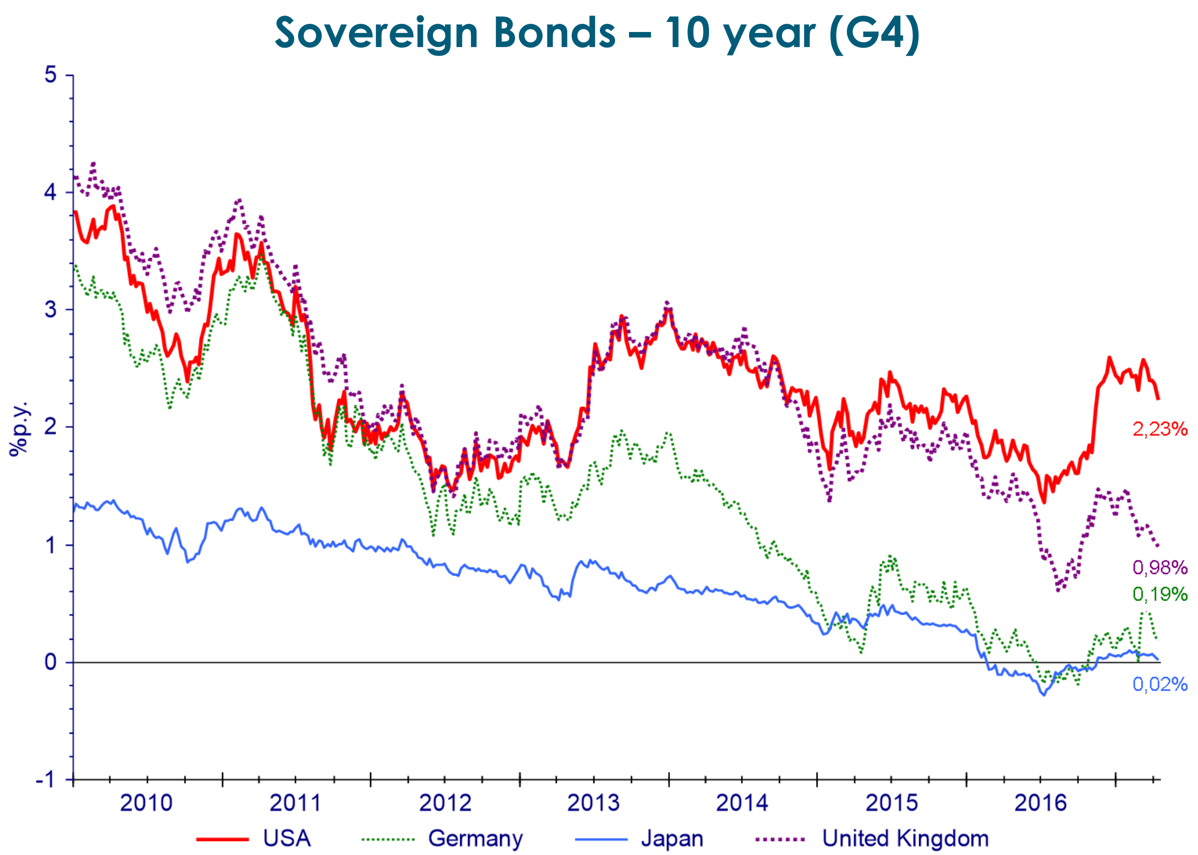
4. Structural Reforms and Resilience

International Context: uncertainty and mitigating factors for some EMEs

- Positive outlook for global economic activity, despite underlying uncertainty
- US tightening with limited impacts on global yields
- Mitigating factors for some EMEs:
    - Terms of trade and commodity prices, despite recent volatility;
    - Resilient capital flows and asset prices;
    - Growth Stimulus in G4 with low inflationary risks: Europe and Japan
- Risks:
    - Sustainability of current growth momentum.
    - Commodities prices volatility
    - Faster than expected MP tightening in advanced economies
    - Protectionism and global growth
    - Outlook for Chinese economy

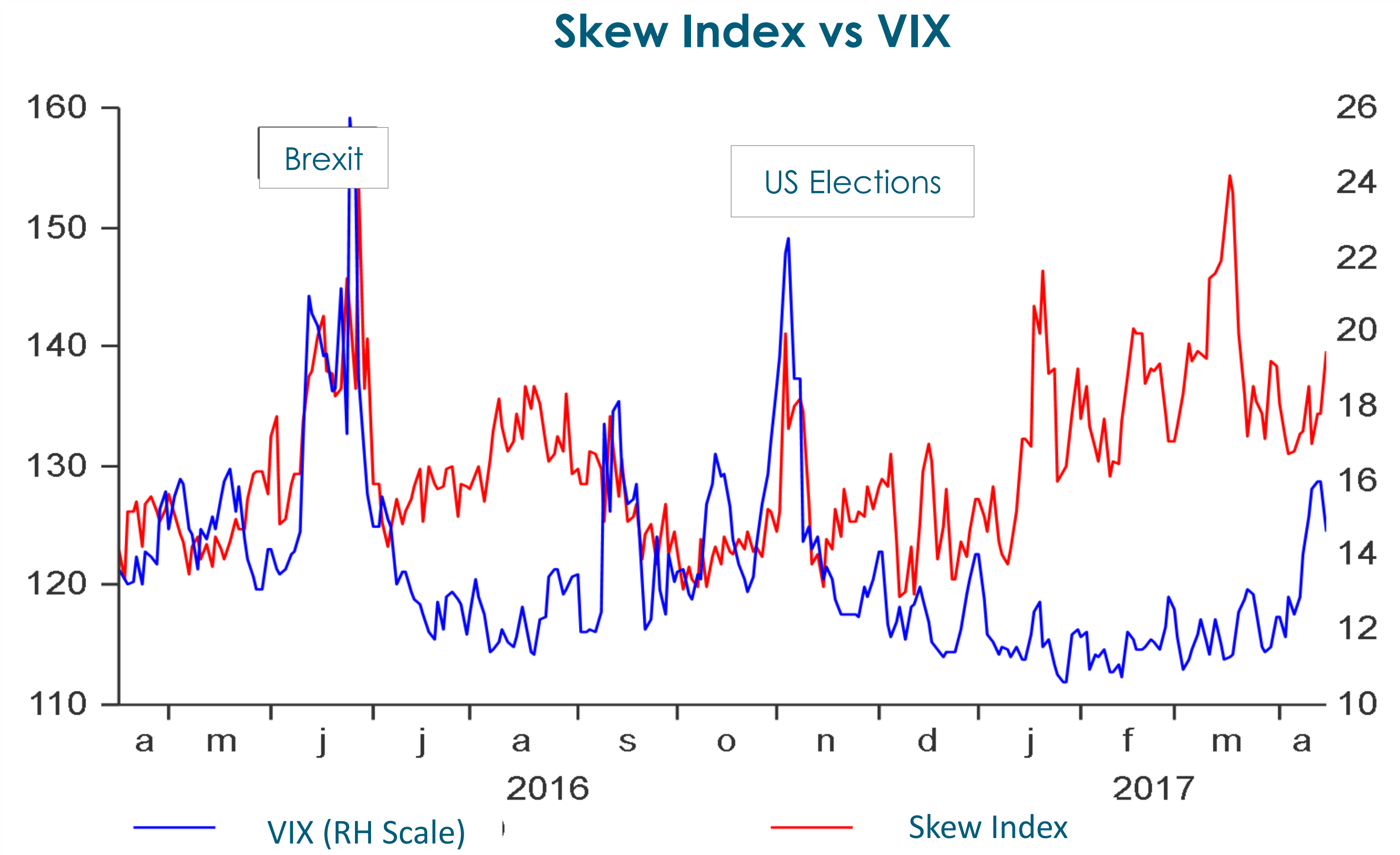
US tightening with limited impacts on global yields





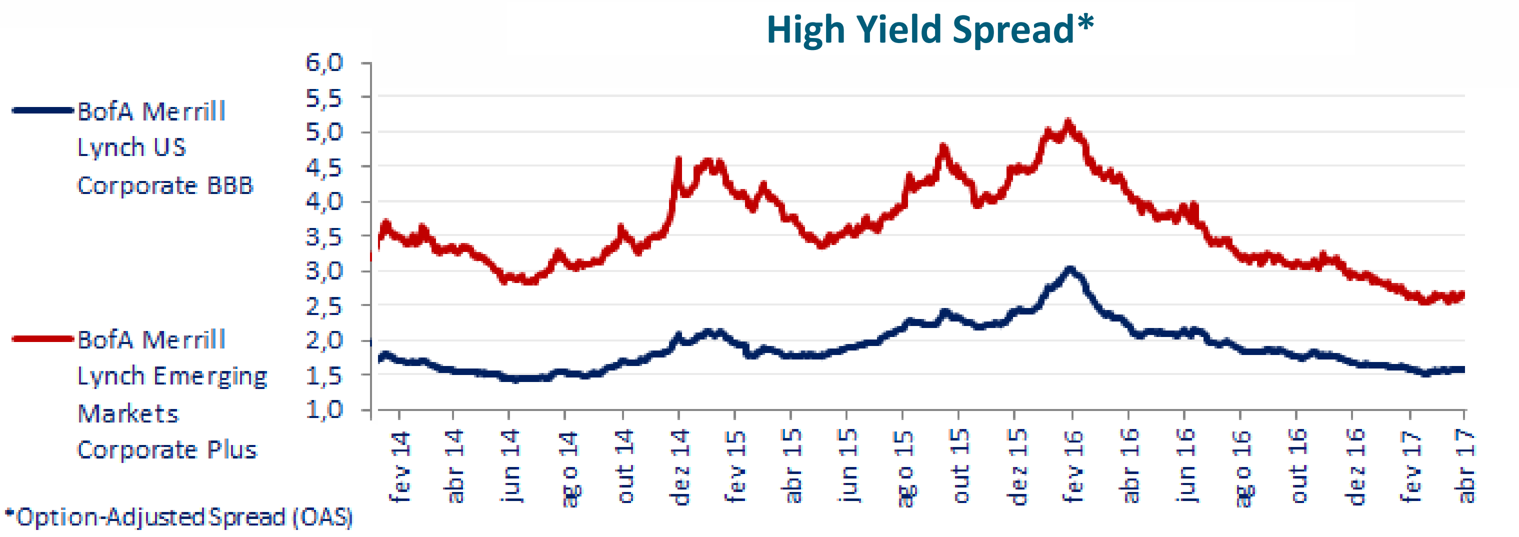
Source: Thomson Reuters Datastream

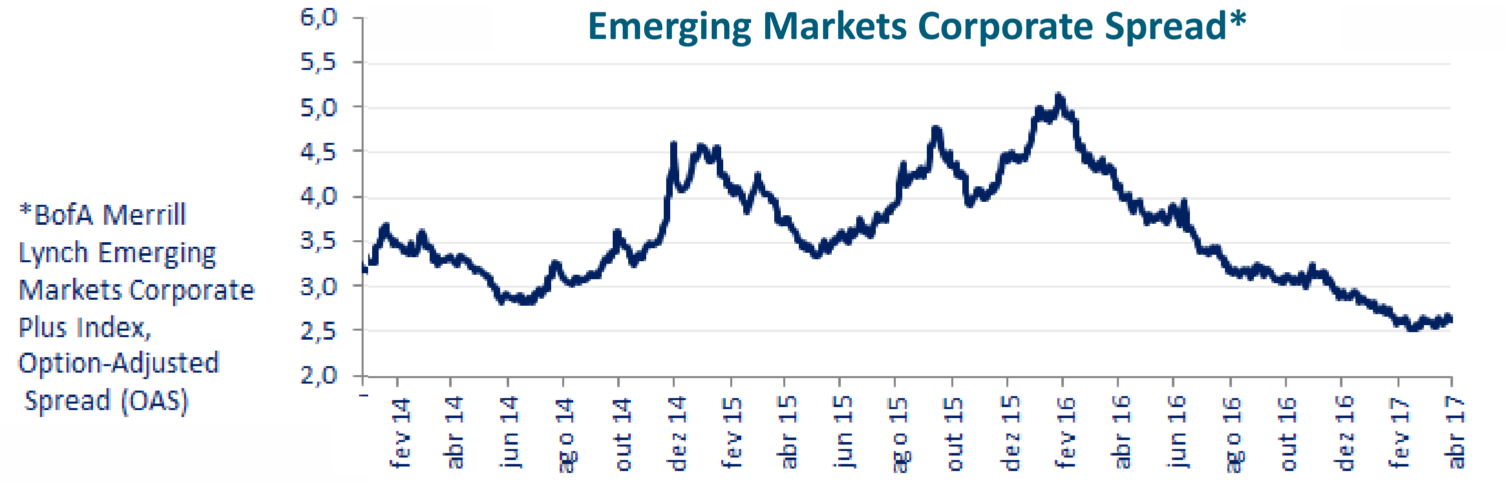
Market Indicators



Source: Thomson Reuters Datastream

Emerging Markets and US Corporative Spreads

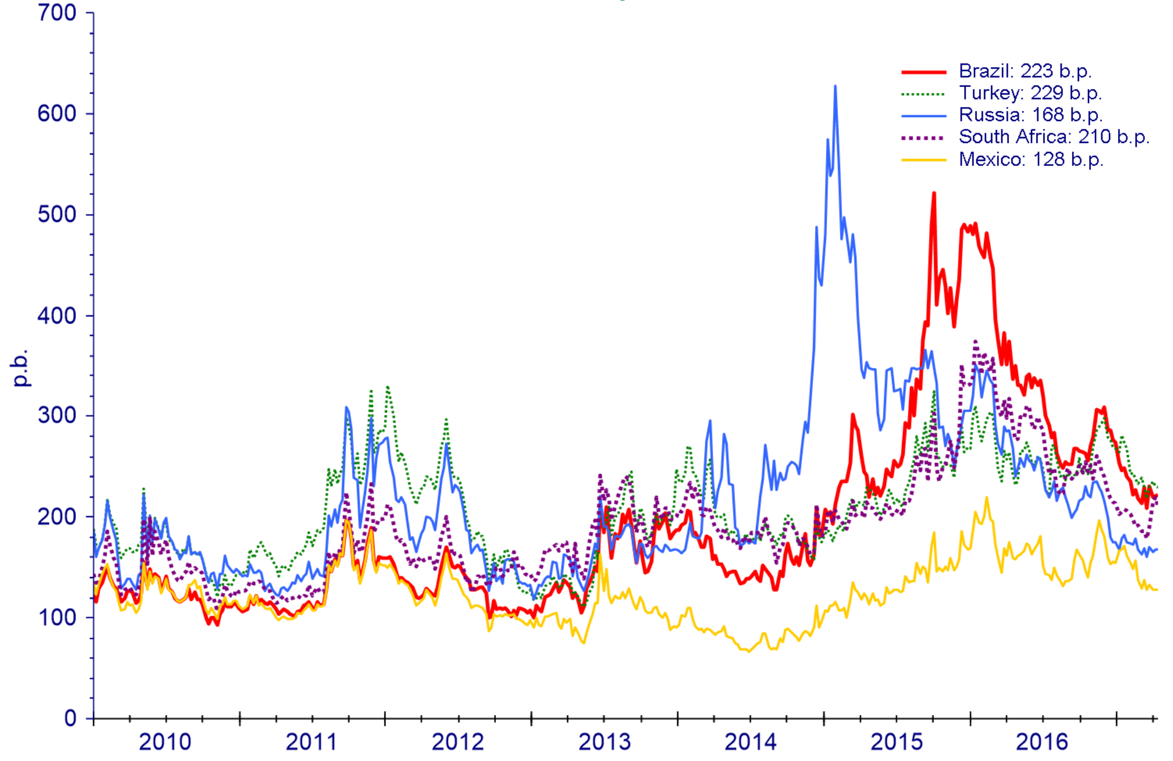




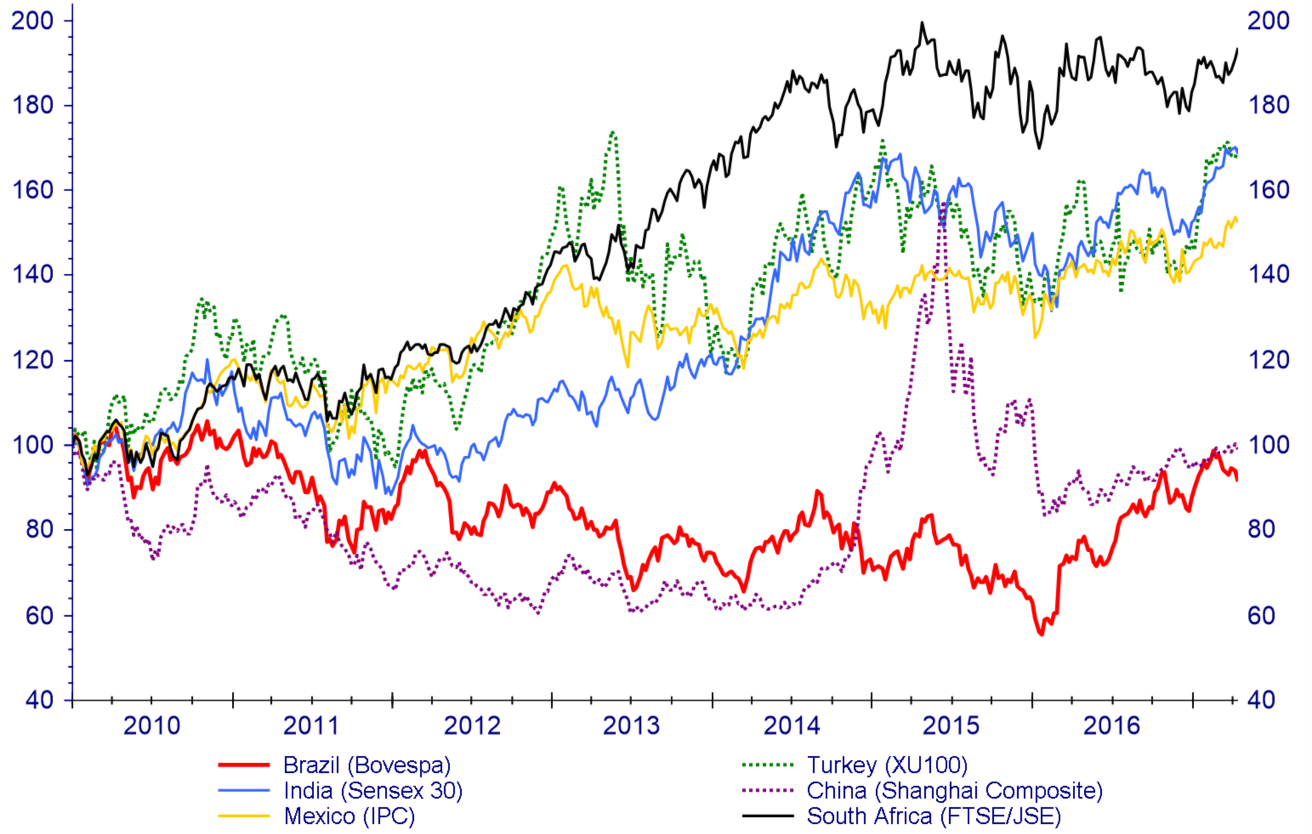
Source: Thomson Reuters Datastream

EME benefiting from better risk perception

CDS Sovereigns
5 year



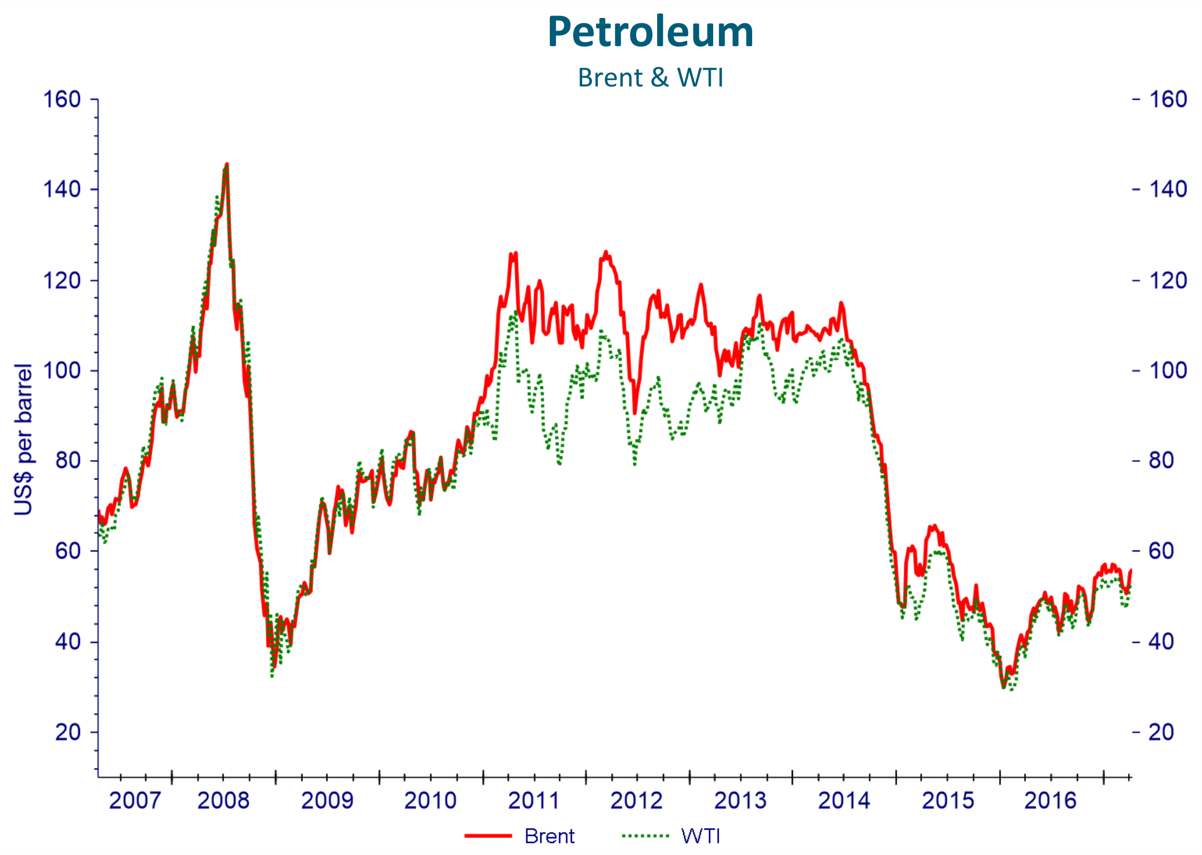
Stock Markets – Emerging Economies
01/01/10 = 100



Source: Thomson Reuters Datastream

BANCO CENTRAL DO BRASIL

Commodity prices



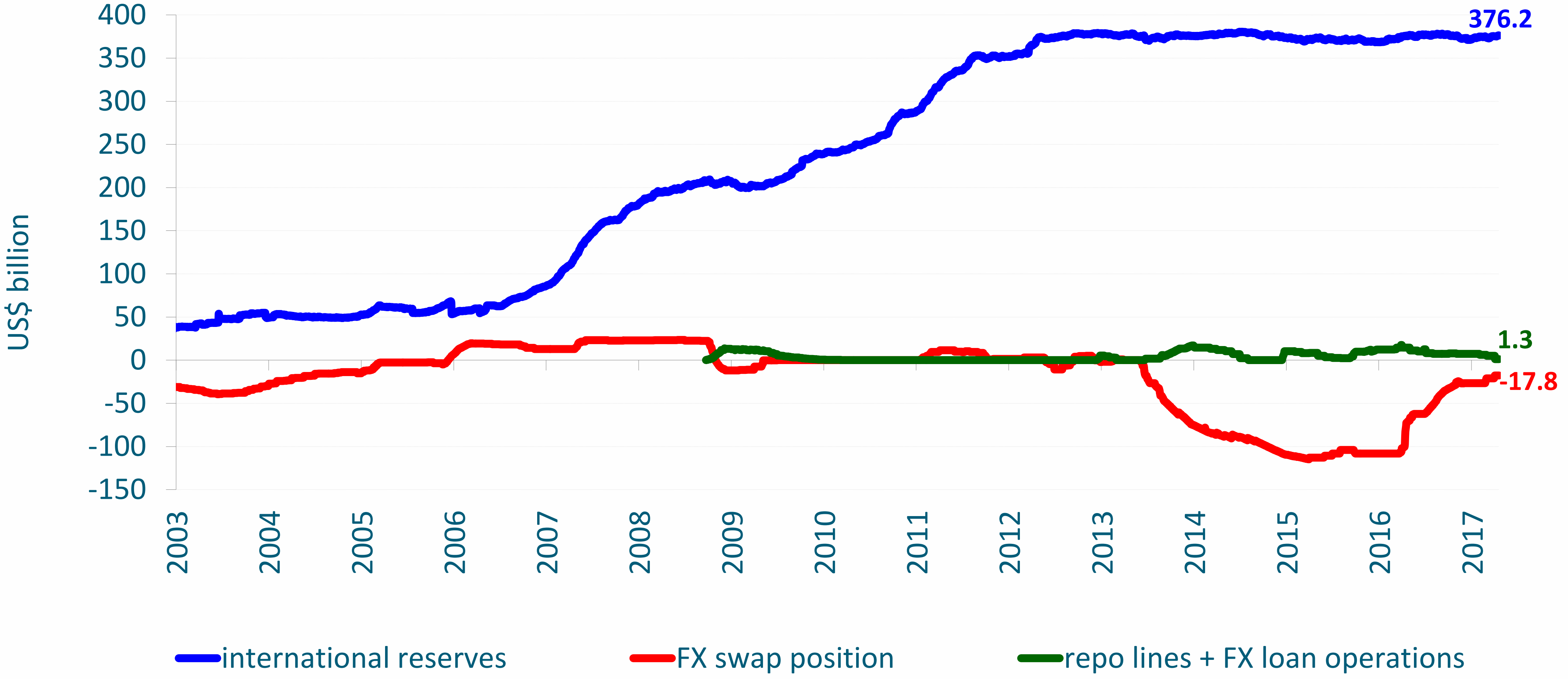
Source: Thomson Reuters Datastream

Brazil in the International Context

- The global outlook coincides with a period of economic stabilization in the Brazilian economy, and improvement in its fundamentals.

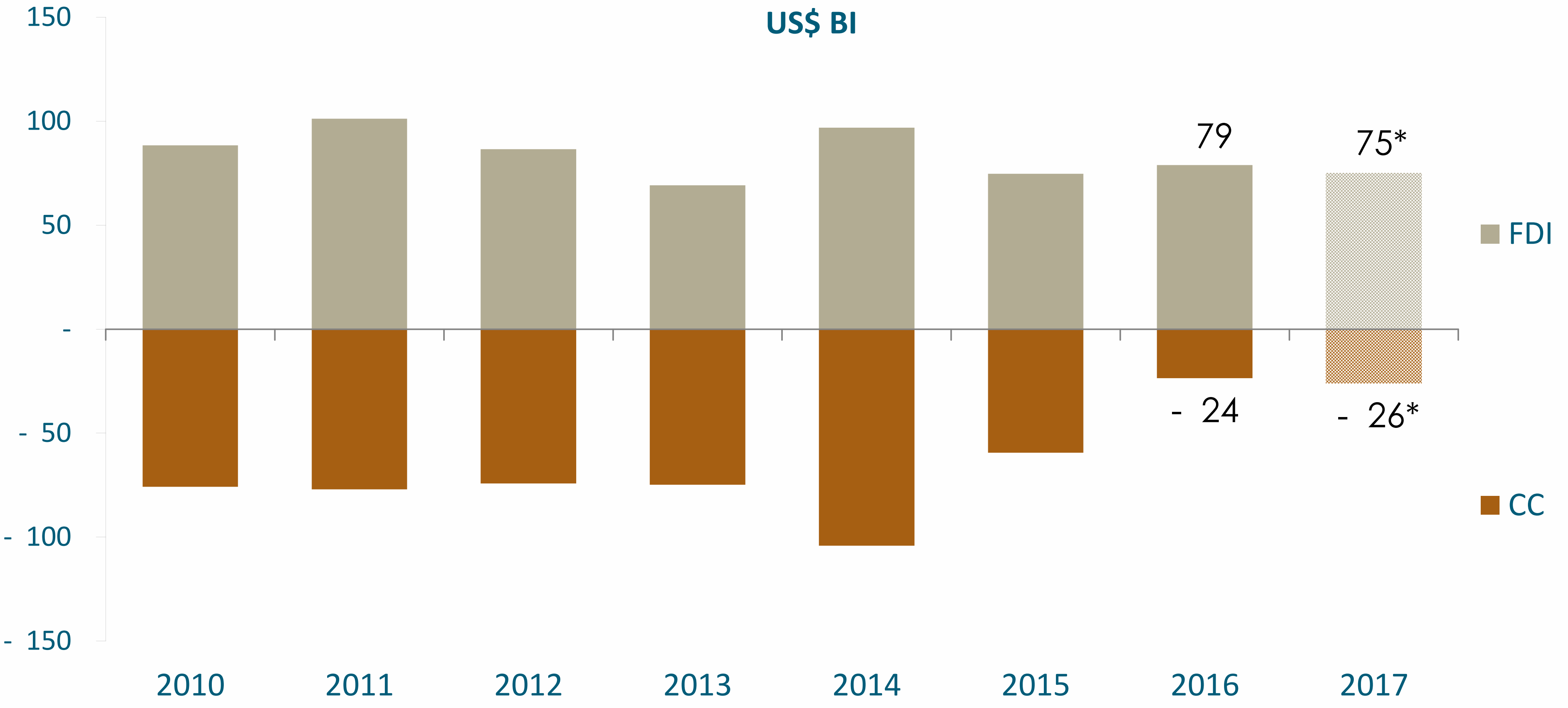
- Brazil is now less vulnerable to external shocks.

Brazil: International Reserves vs. FX Swap and Repo Lines or FX Loans



Source: BCB *through April 19th

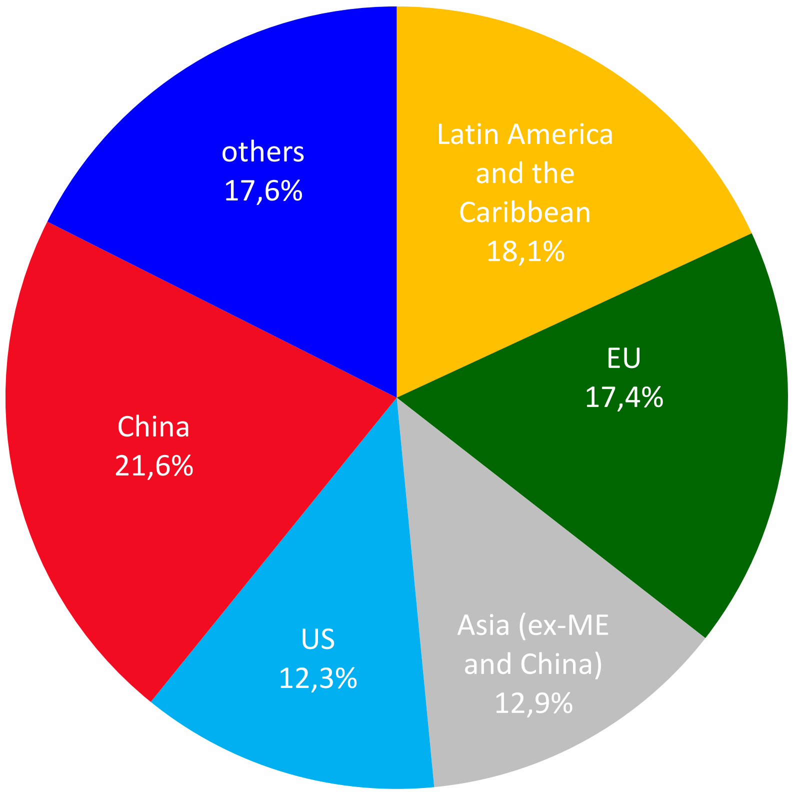
Brazil: Current Account x FDI



Source: BCB

*Market Expectations – Focus Report, Apr 13th - 2017

Brazil: Exports by Destination

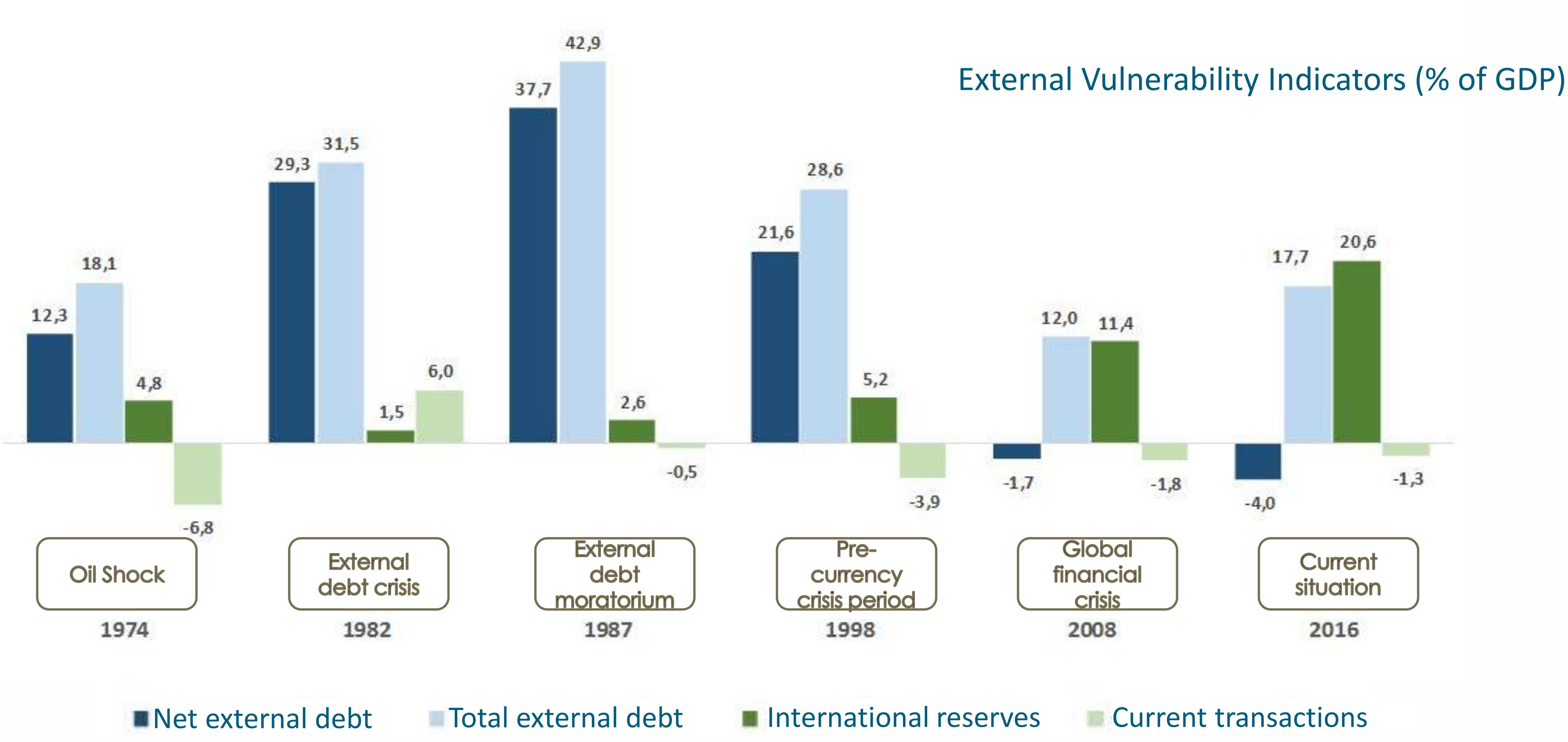


	12m until Feb/17
	Exports/GDP
Total exports	**10.1%**
Latin America and the Caribbean	1.8%
European Union	1.8%
Asia (ex-ME and China)	1.3%
USA	1.3%
China	2.0%
others	1.8%

Mar/16 – Feb/17: US$191.0 billion
Apr/16 – Mar/17: US$195.1 billion

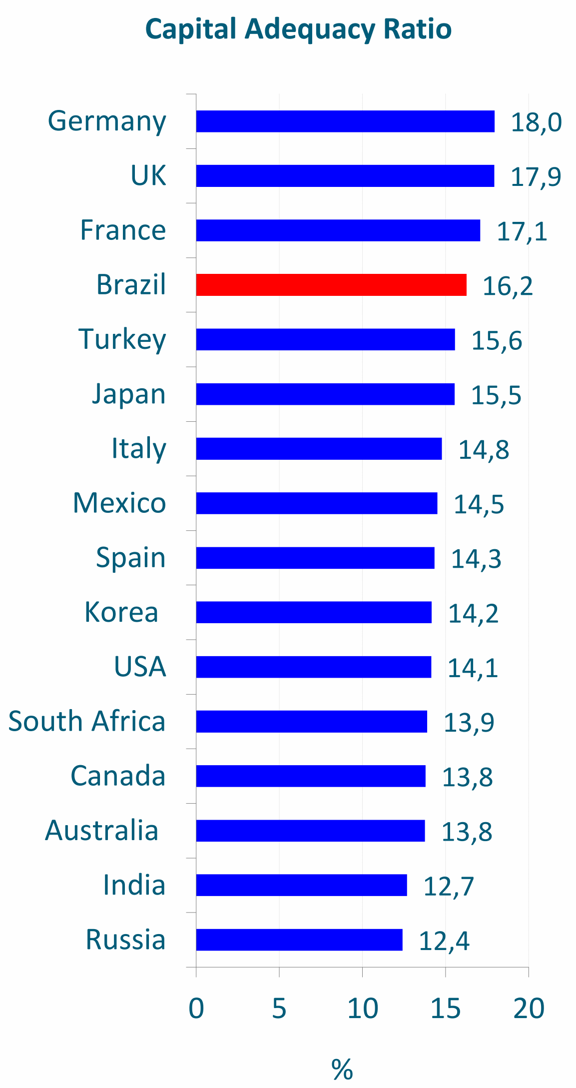
Source: BCB

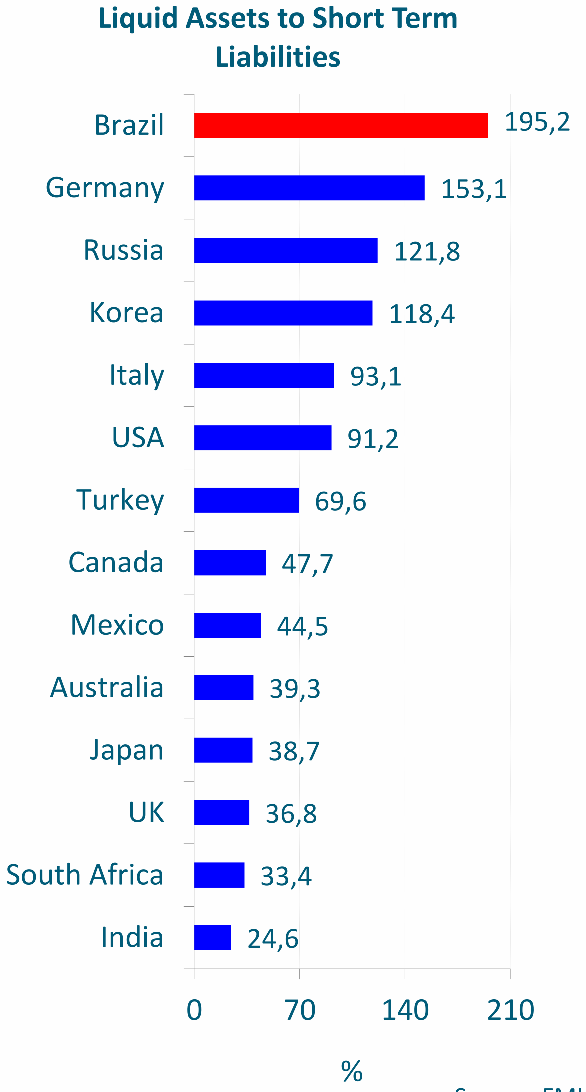
Reduction of External Vulnerability



Source: BCB, National Treasury Secretariat

Financial Soundness Indicators





Source: FMI (FSI) – latest available data

BANCO CENTRAL DO BRASIL

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2. Growth Dynamics: stabilization and signals of recovery

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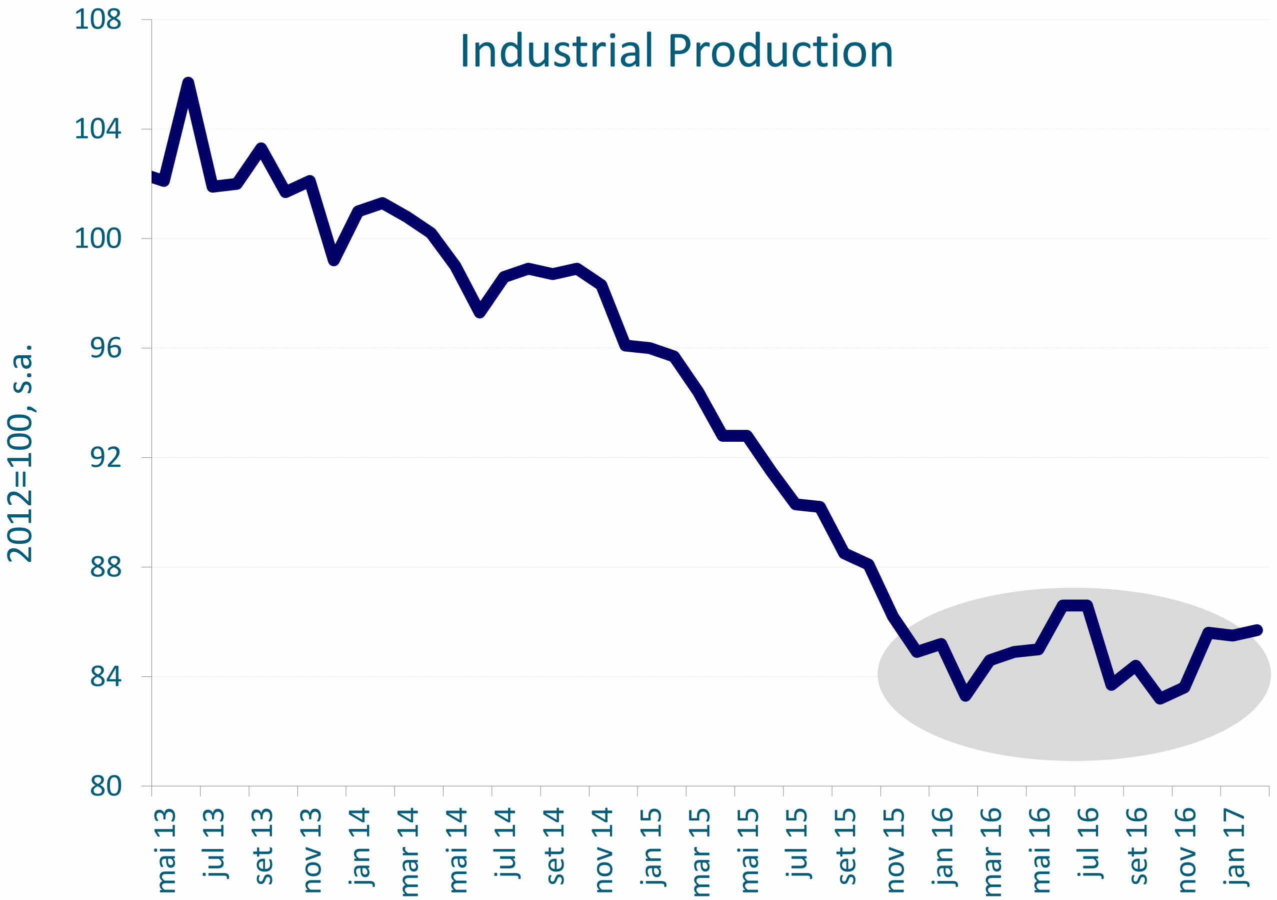
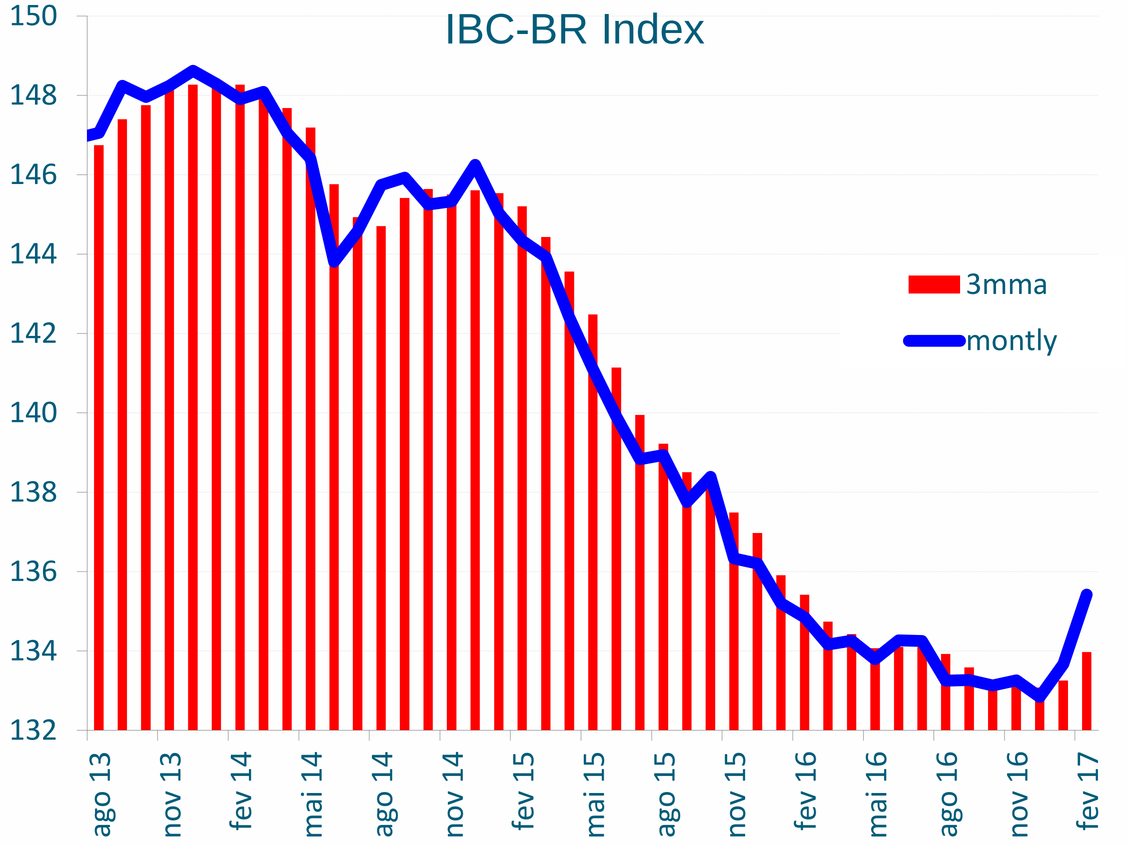
Stabilization and signs of gradual recovery

- Recovery in businessmen confidence indexes
- Monetary Policy easing cycle
- Deleveraging process well advanced
- Strong growth in agricultural sector
- Infrastructure Concessions. Asset Sales and Privatization Agenda. Concessions to the Private Sector: Logistics Investment Program (PIL) and Infrastructure Works with regulatory stability
- Business Climate improvement and efficiency and productivity gains
- Structural Reforms (government expenditure cap, social security, tax and labor reforms)

Industrial Production and IBC-BR Index





Source: IBGE

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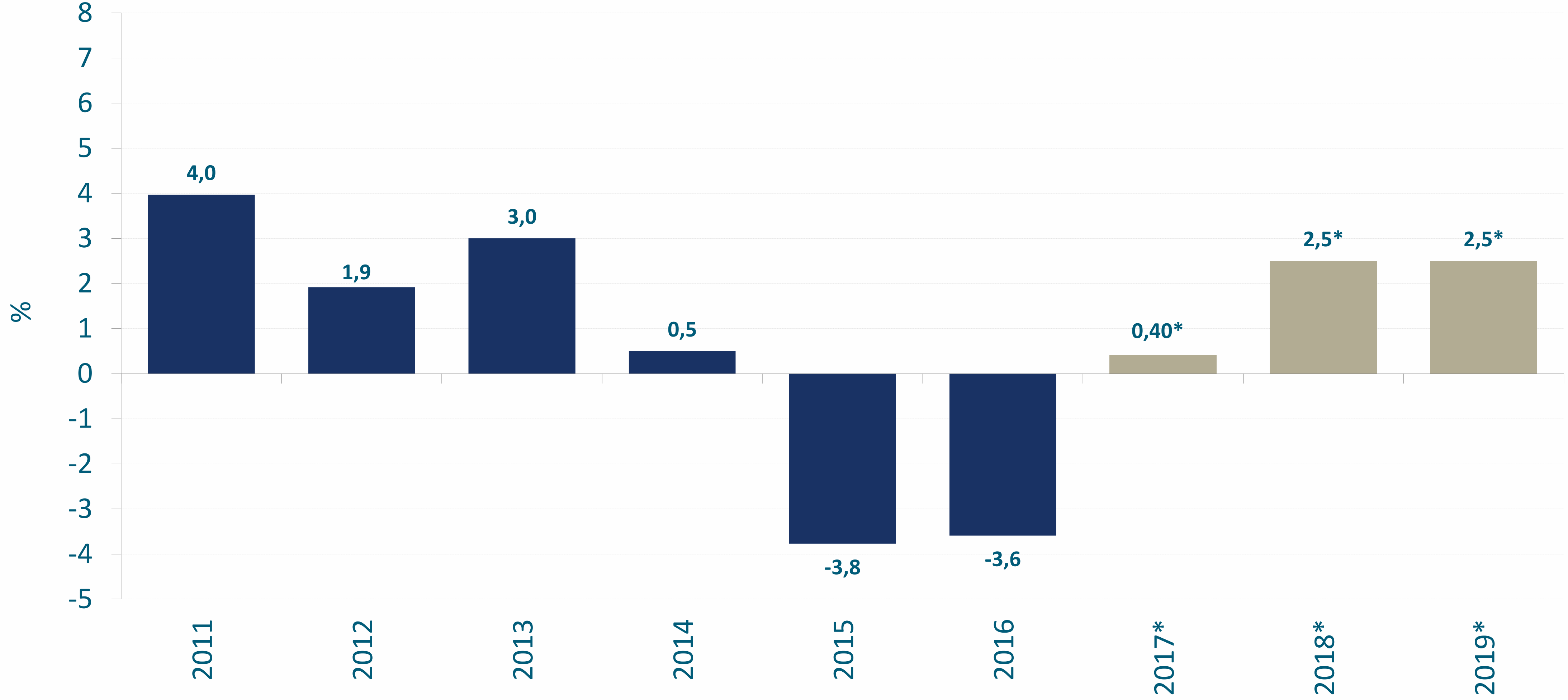
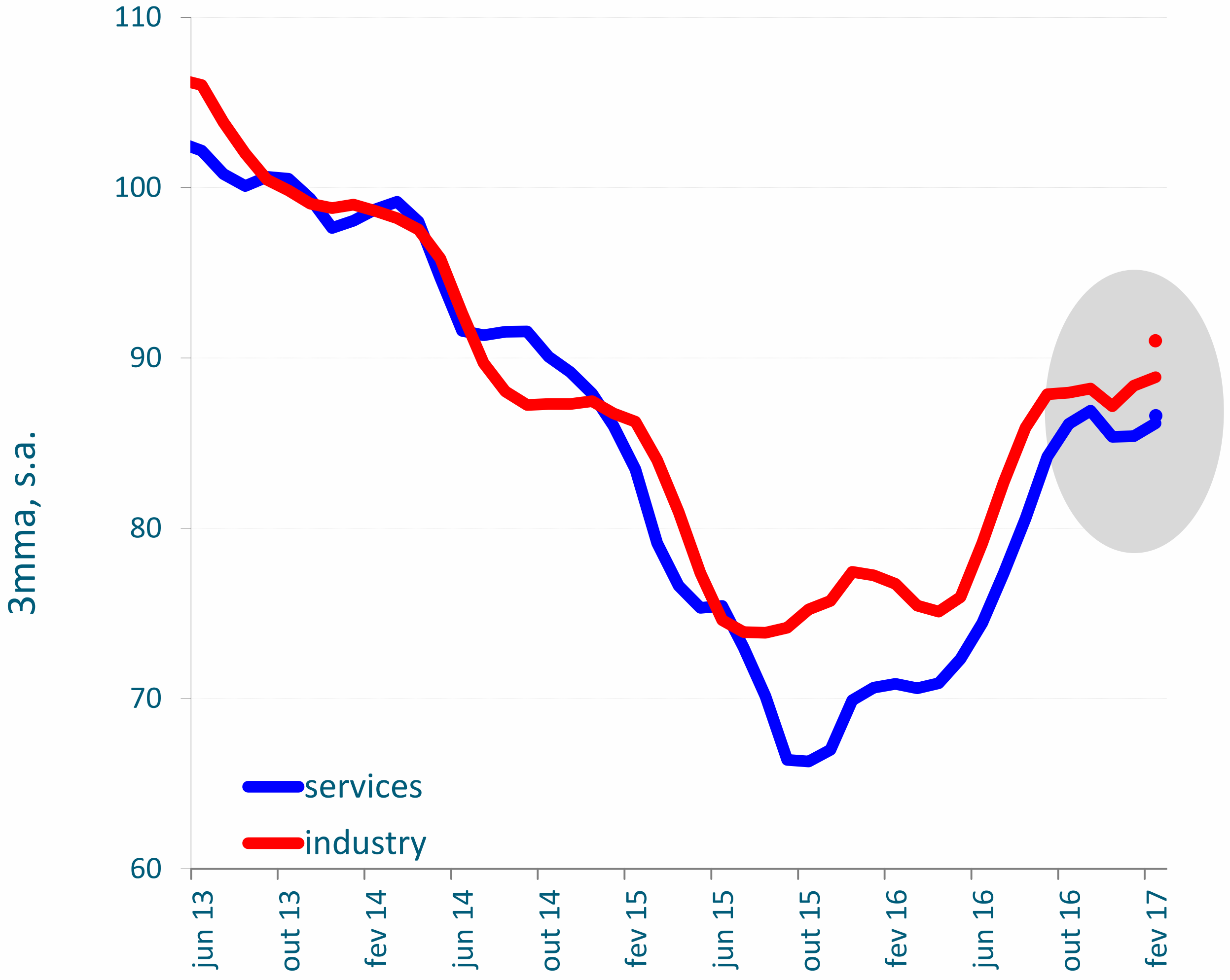
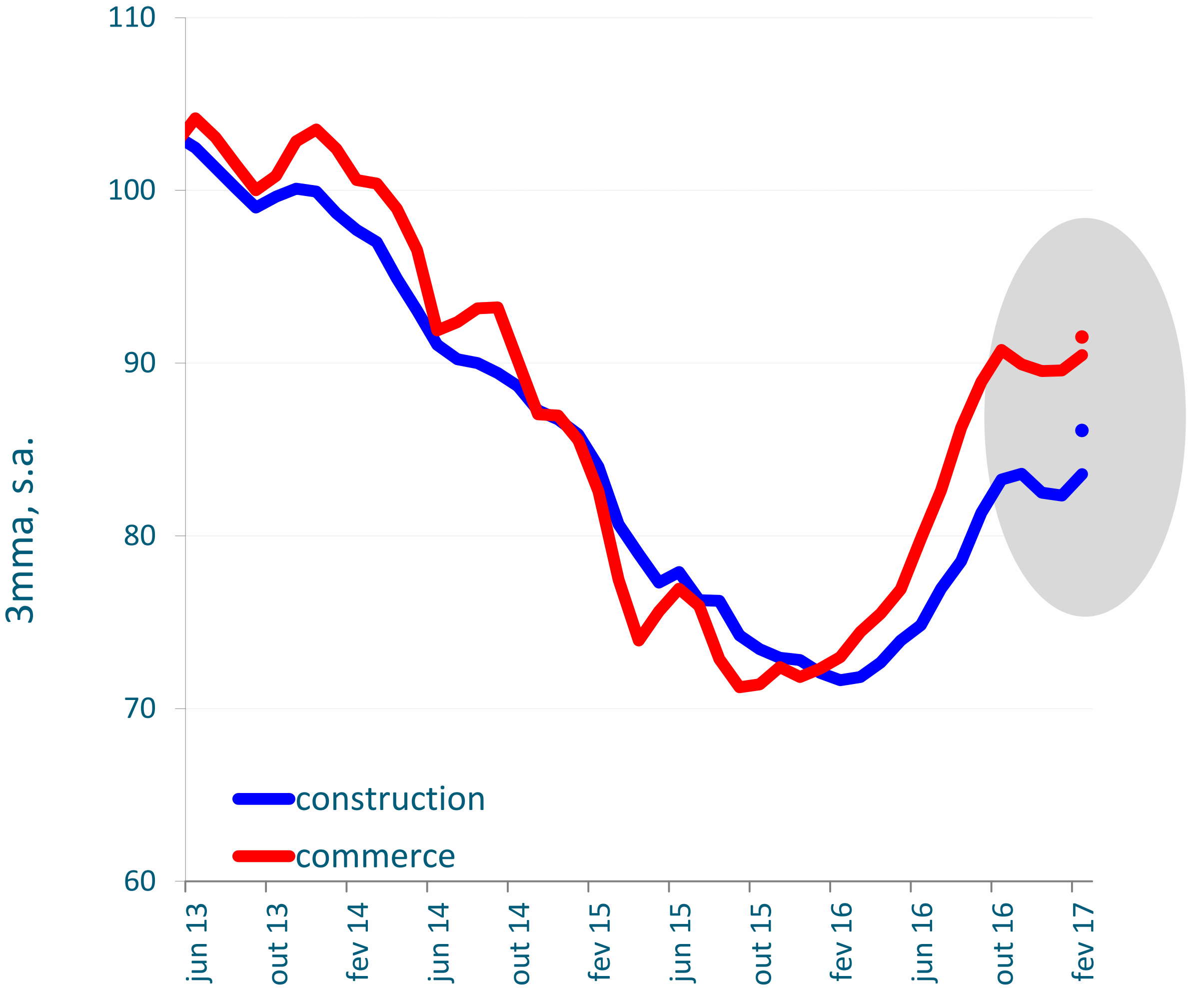
GDP Real Growth



Sources: BCB / IBGE *Market Expectations – Focus Survey of Apr 13th

Agents' Confidence - Businessmen

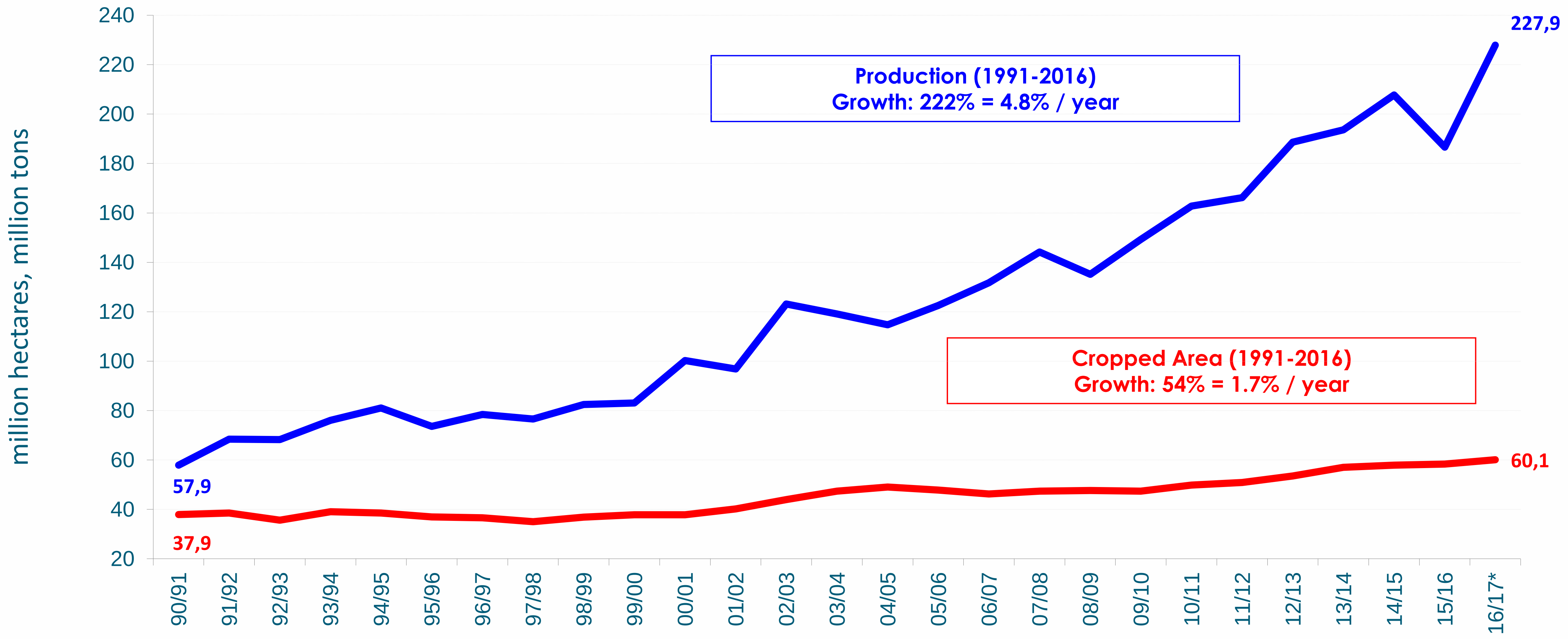




Source: FGV

Obs.: proportion of favorable answers – proportion of unfavorable answers + 100

Grains, Production and Cropped Area

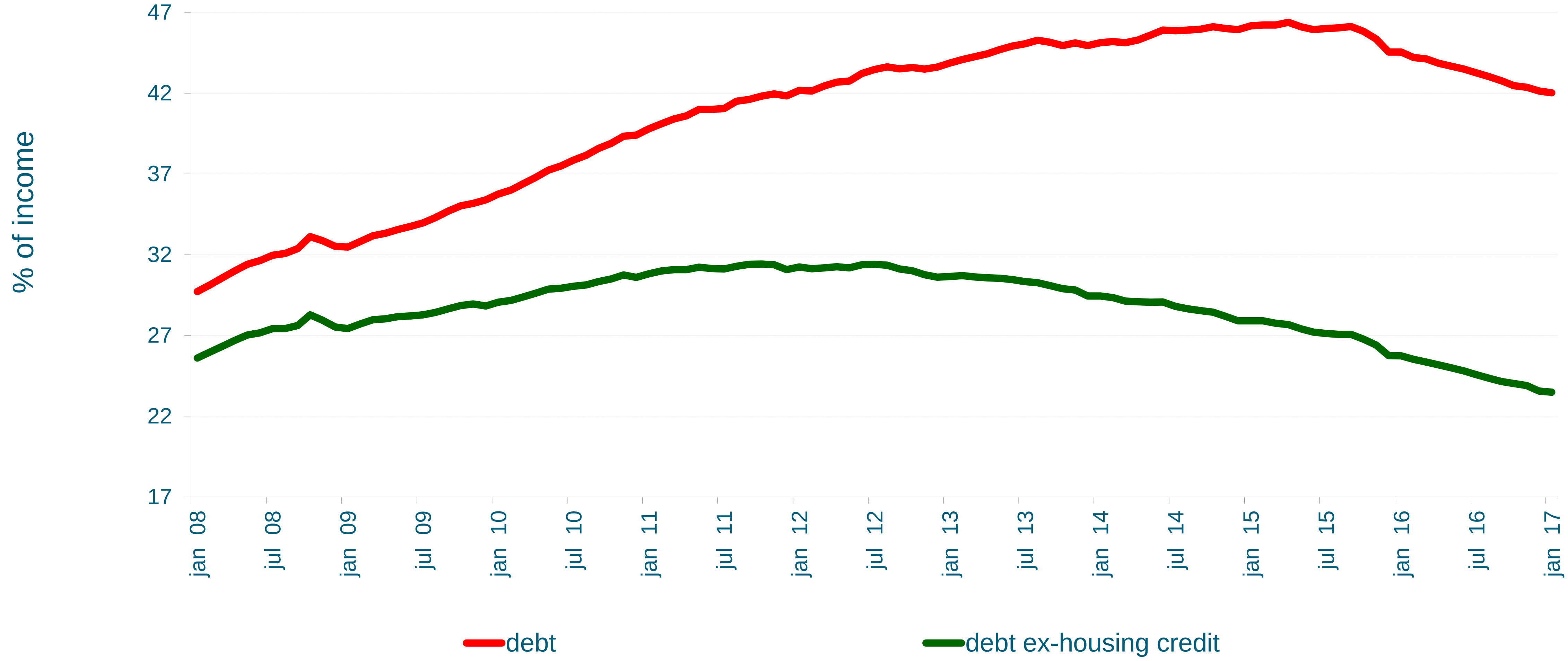


Source: Conab

*average estimate in Apr 17

Deleveraging Process (I)

Household Debt



Source: BCB

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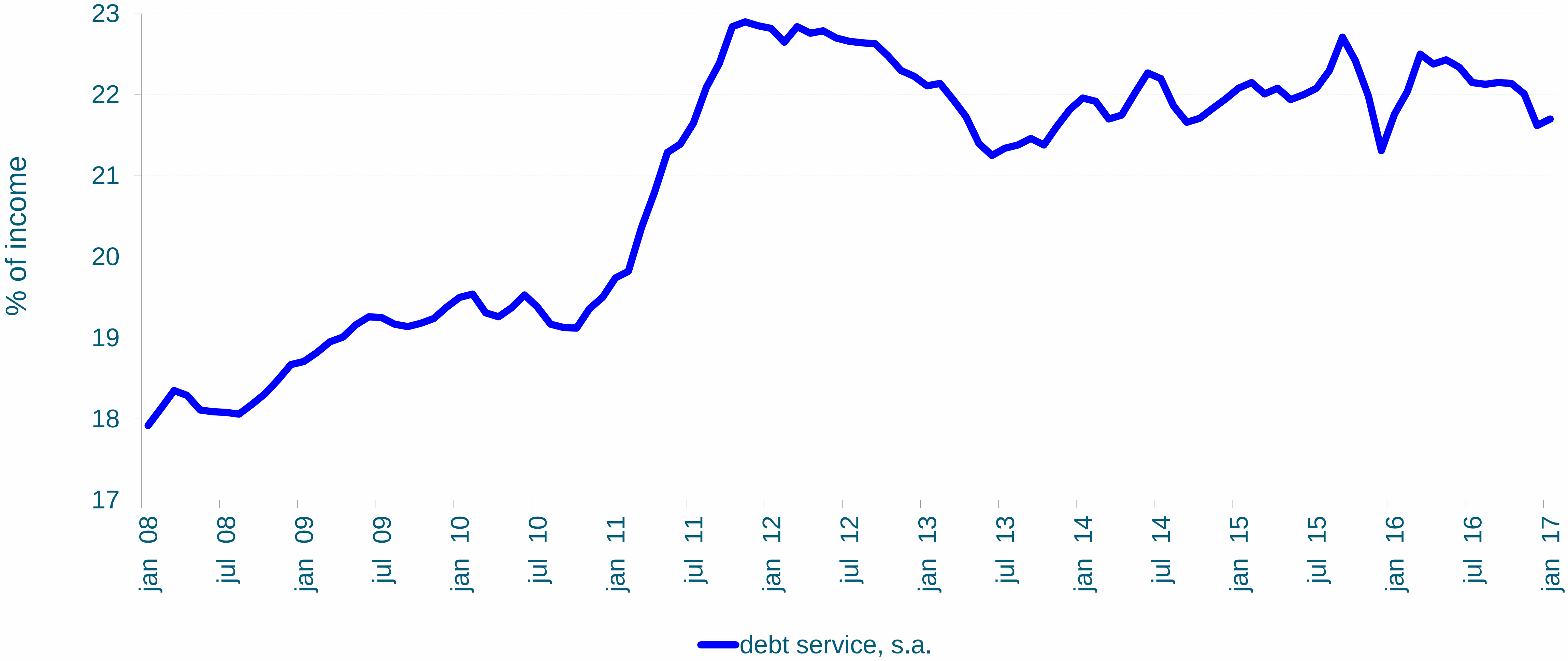
Deleveraging Process (II)

Debt Service



Source: BCB

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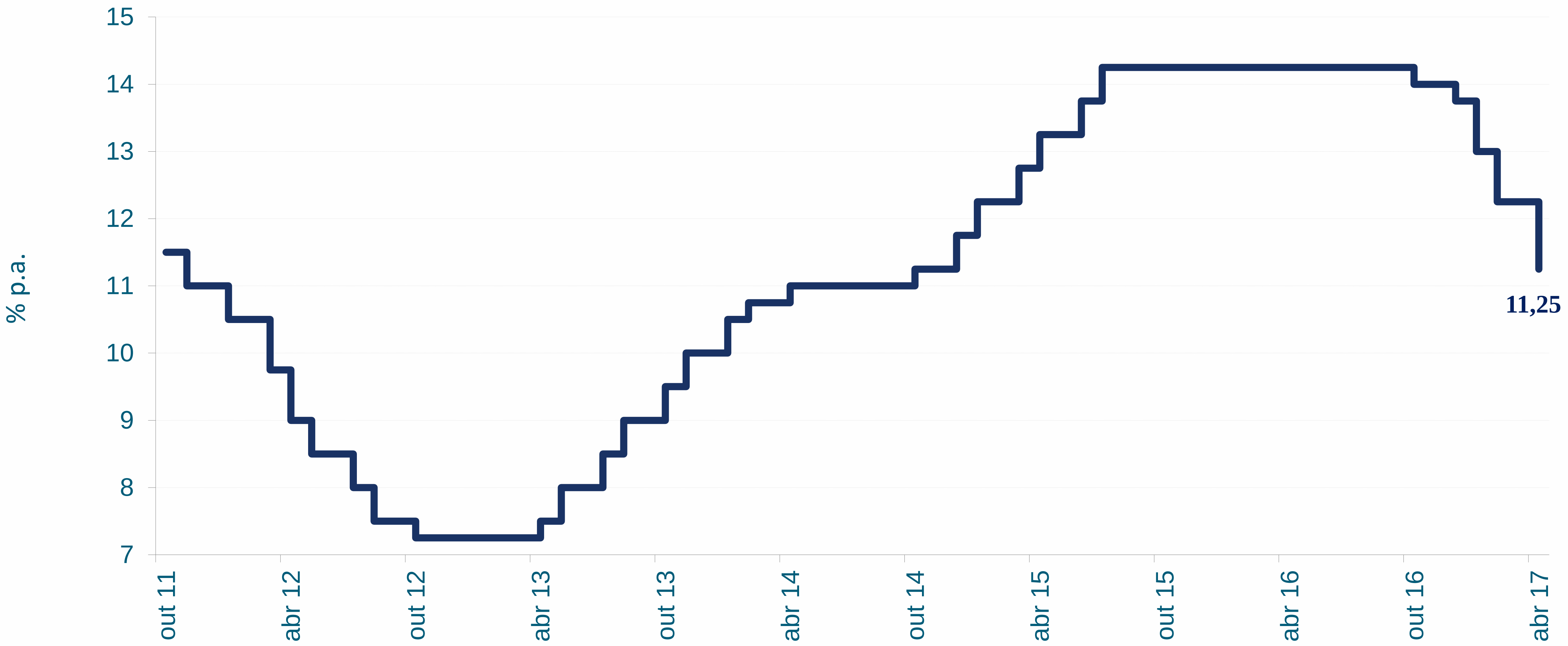
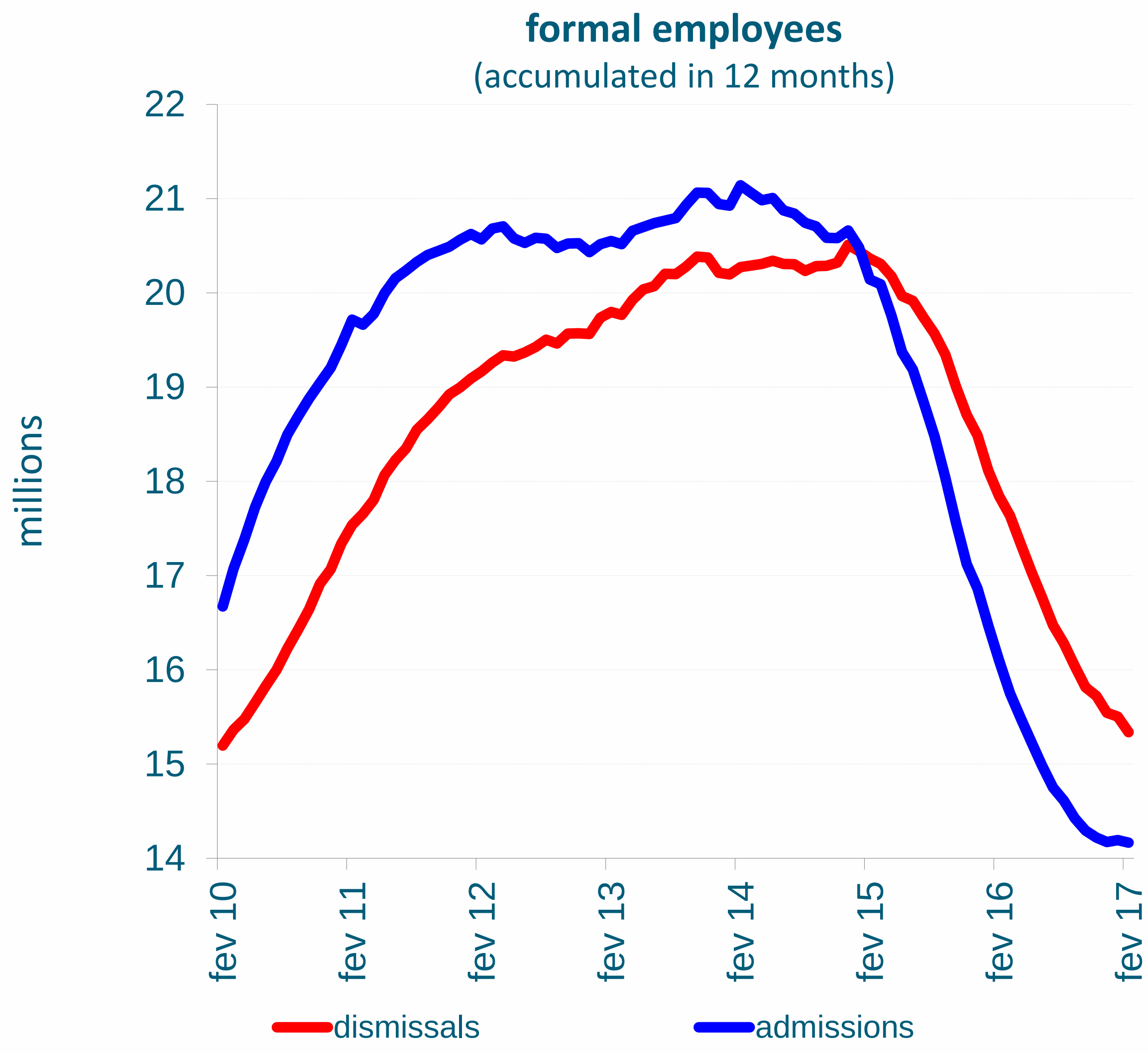
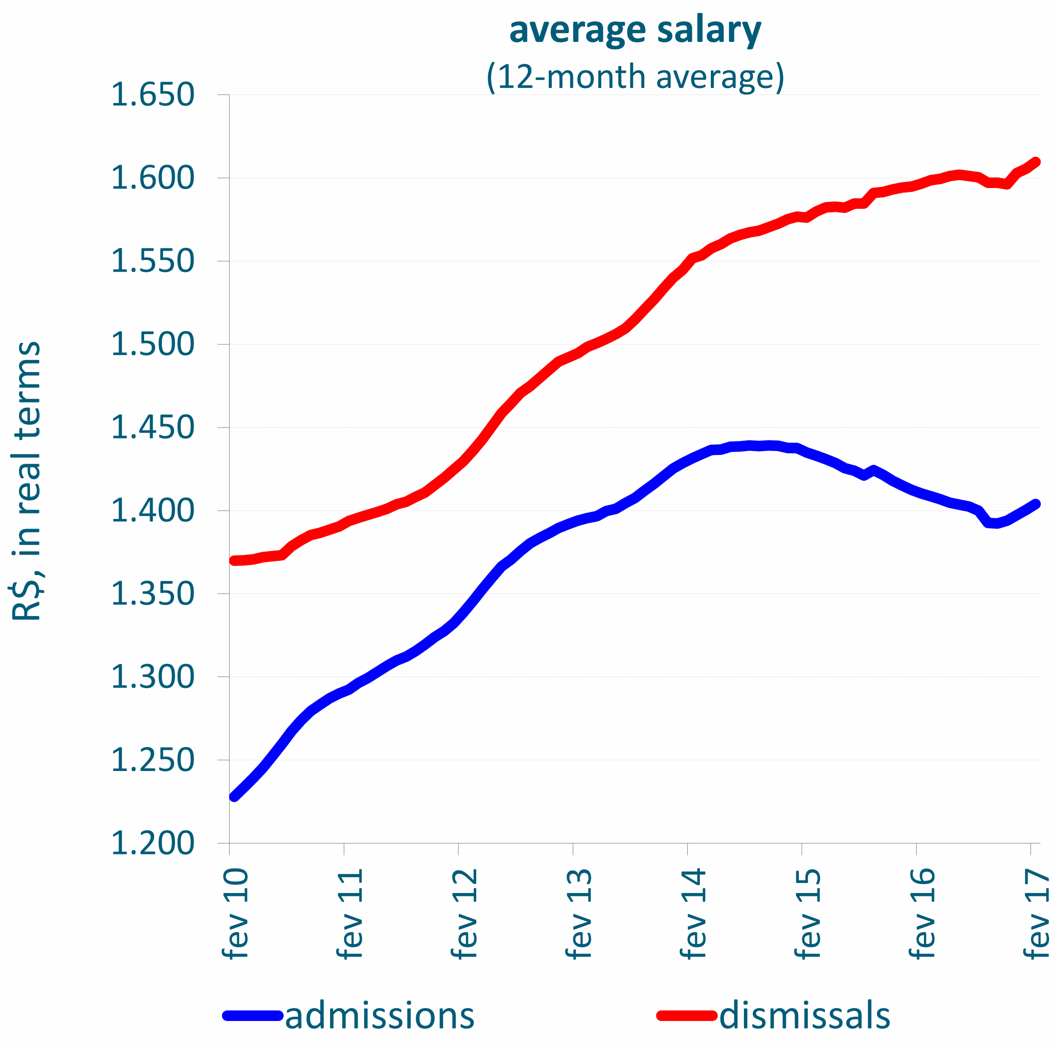
Selic Rate



Source: BCB

Admissions and Dismissals vs. Salaries





Sources: MTPS (CAGED) / IBGE (INPC)

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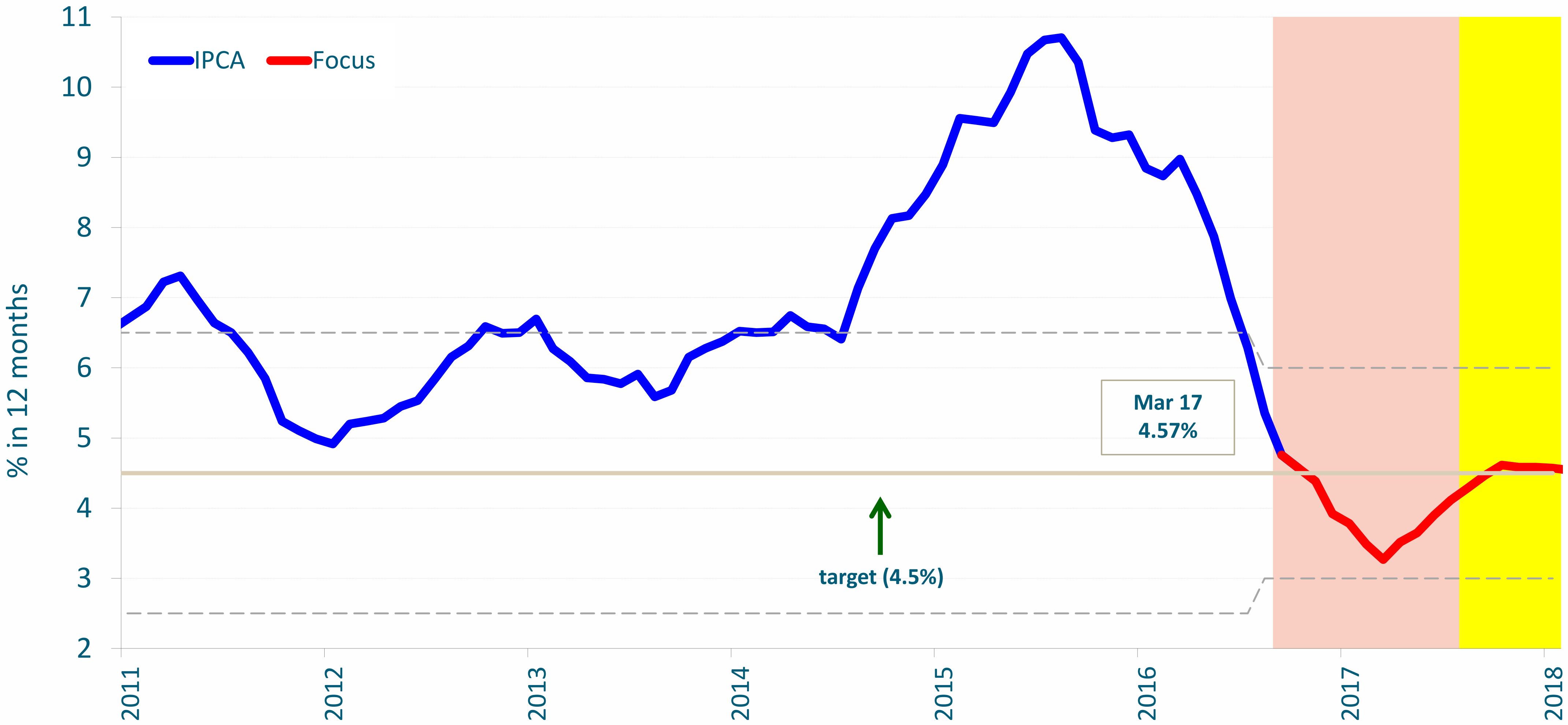
Monetary Policy Outlook: Inflation and current easing cycle

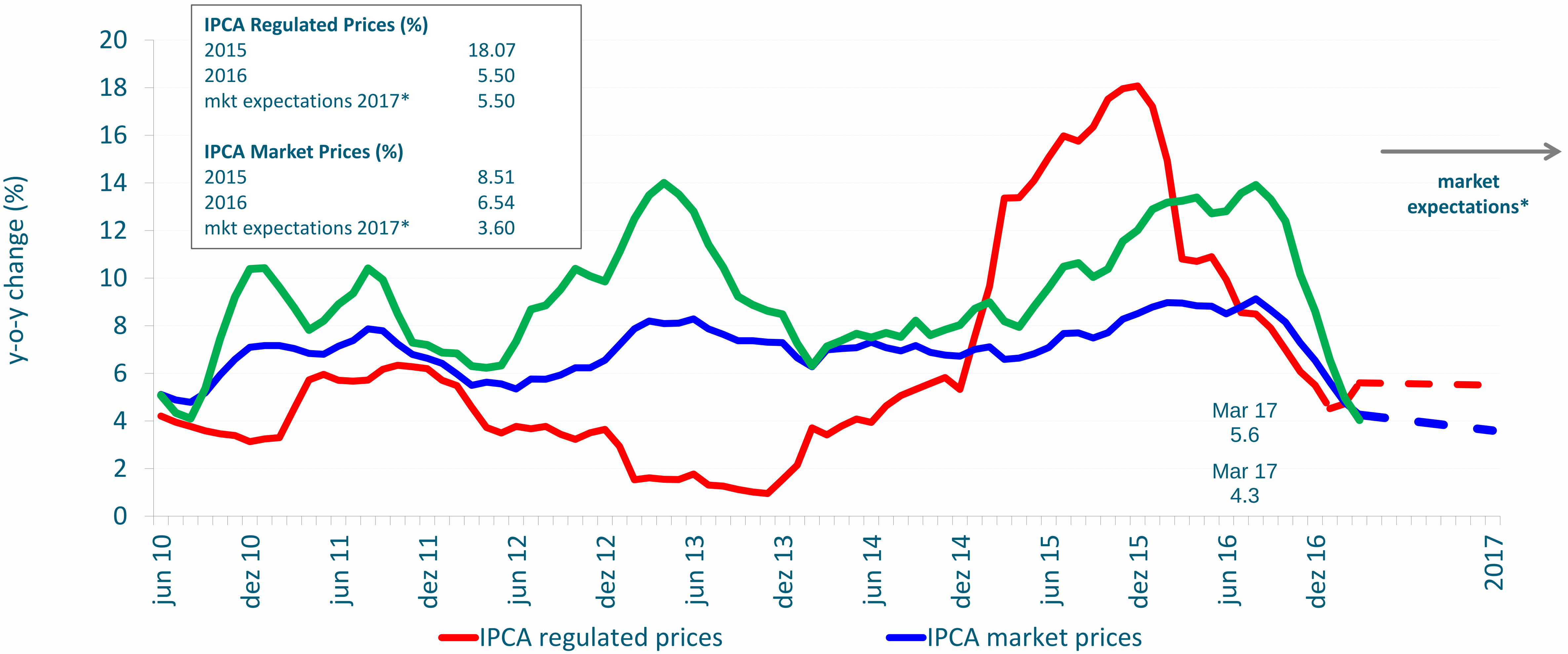
- Consolidation of a disinflation for inflation components that are most sensitive to the economic cycle and to monetary policy justified a moderate intensification of the monetary easing process. The Committee judged the pace of 100bps adequate.
- IPCA diffusion indexes exhibited a relatively large drop in recent months
- Favorable inflation dynamics, with widespread disinflation, lower persistence and expectations well anchored in longer horizons.

Consumer Price Inflation (IPCA)



Source: BCB, Focus
Focus: expectations as of Apr 13th

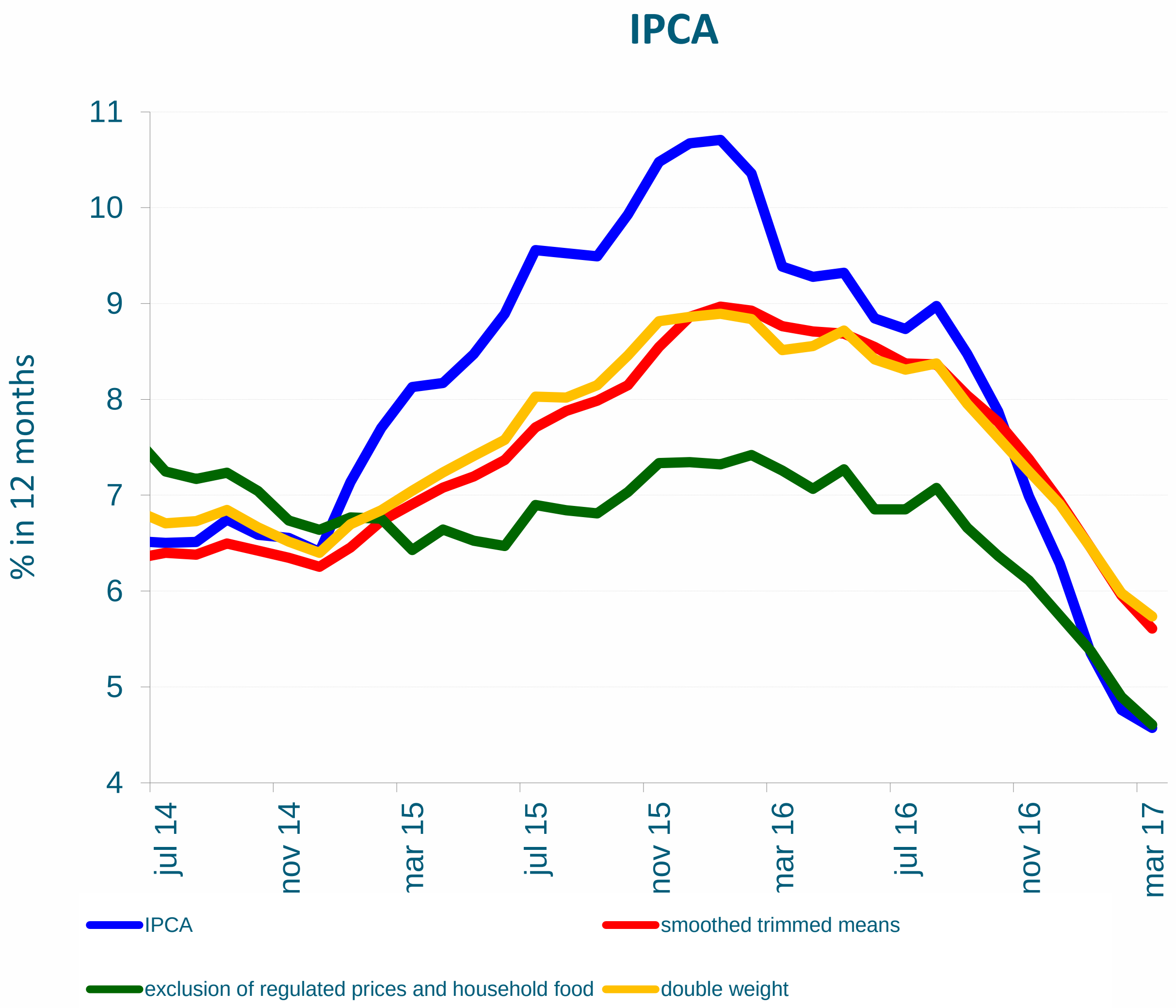
Market, Regulated and Food Prices

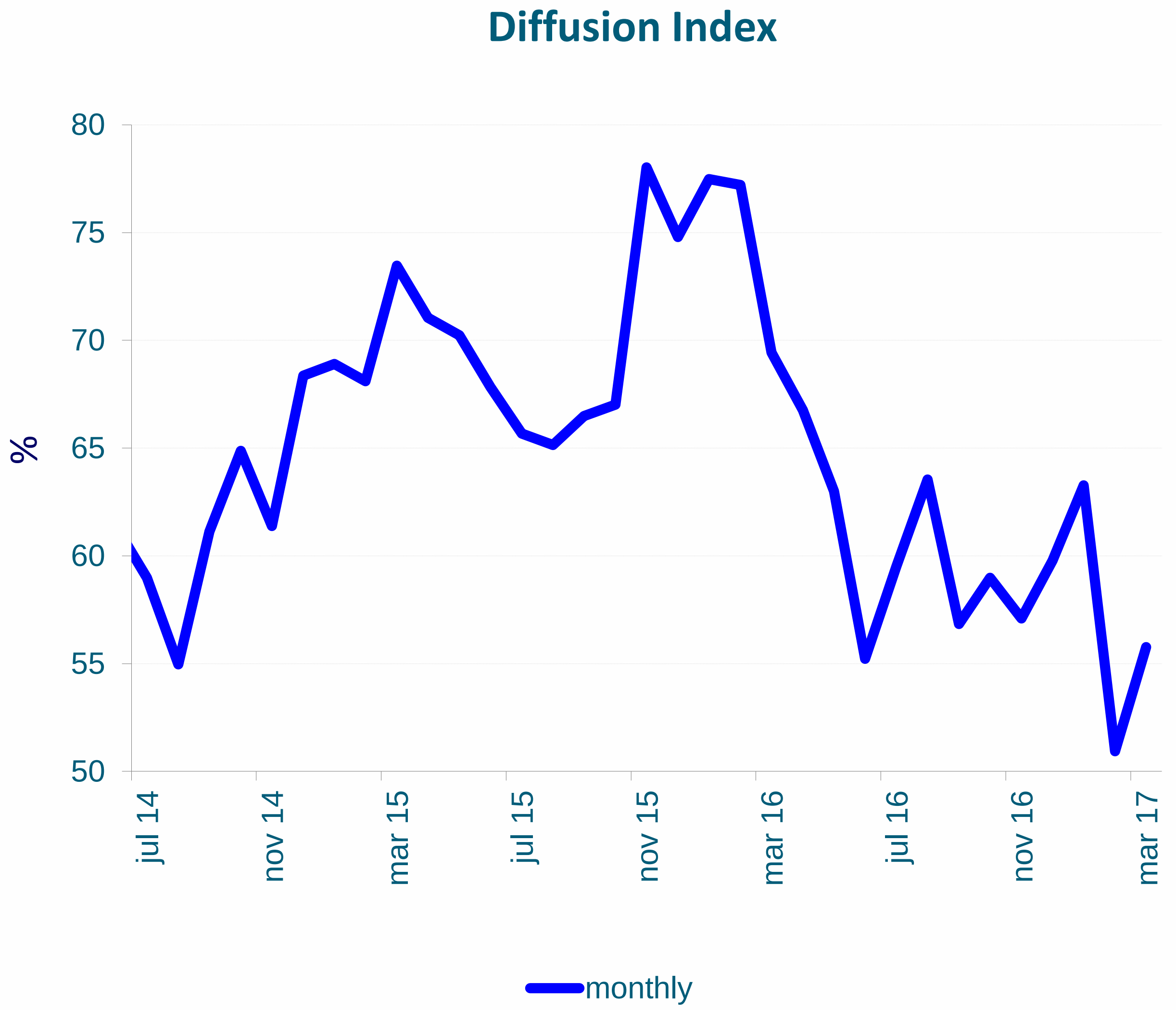


Sources: BCB, IBGE

*as of April 13th

IPCA – Headline, Cores and Diffusion Index





Source: IBGE

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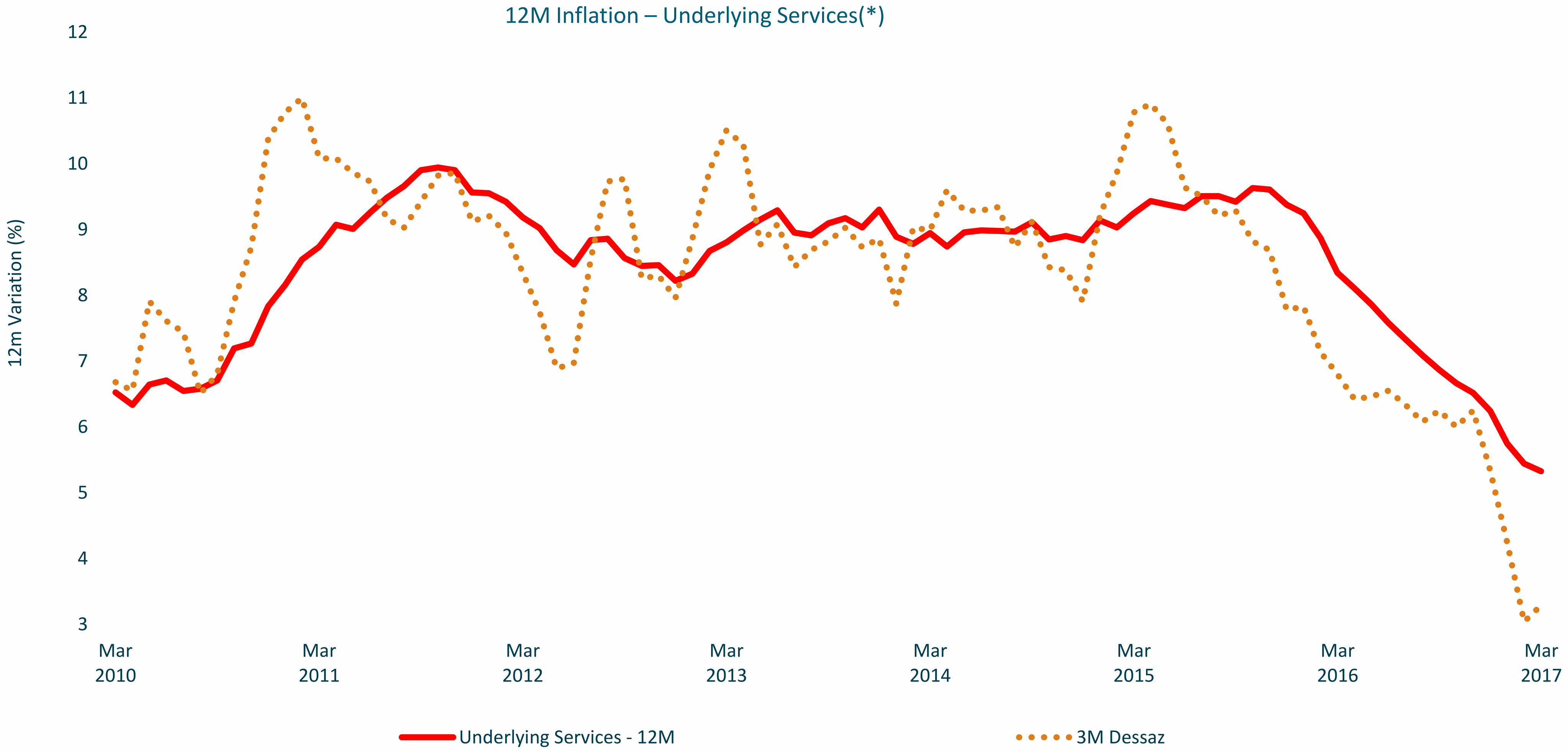
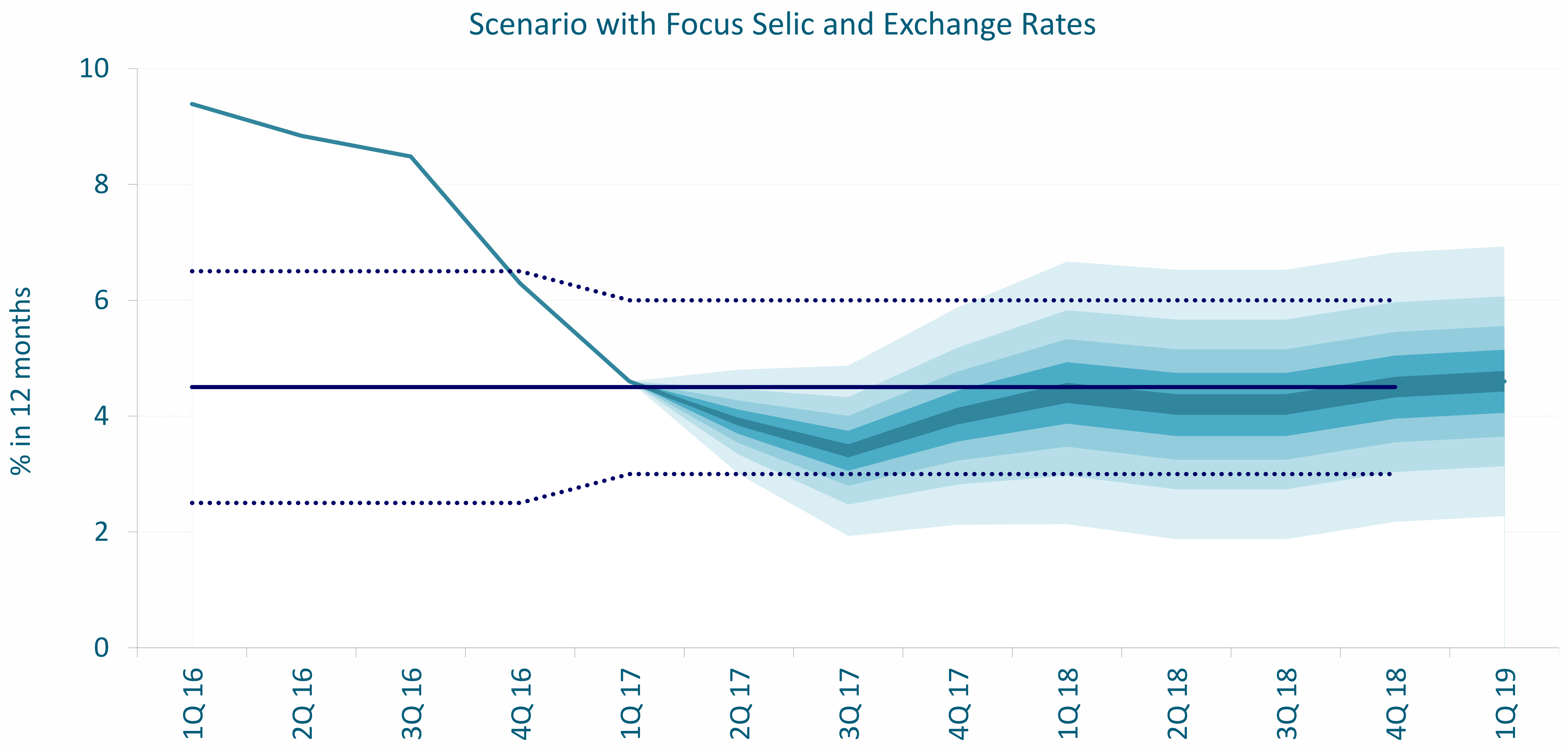
Services Prices Path (CPI-IPCA): Underlying Component (moving average)



Source: BCB

(*) Overall services excluding domestic services, courses, communication and tourism.

Conditional Inflation Forecasts



Source: BCB

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4. **Structural Reforms and Resilience**

Business Environment Improvement

- Microeconomic Measures
  - Measures to support the reduction of margin on bank loans
    - Streamline credit worthiness list (Cadastro Positivo)
    - System for Electronic Receivables
    - Creation of Central Bank work force to investigate spread reduction
  - Real-estate market
    - Enhance the credit market with creation a mortagage-back security (LIG)
  - Cut time to open new companies
  - New BNDES Policy
    - Working capital credit line (BRL 5 bn to direct operations and BRL 8 bn ton indirect ones)
    - SME classification change: from BRL 90 to BRL 300 mi in gross operating revenue/year
    - Incentives to integrate different industries
    - Monitoring and evaluation of results
  - Government Severance Indemnity Fund for Employees - FGTS
    - FGTS investment fund new selection rule based on strict project finance
    - Withdrawal authorization for inactive employees' accountant: estimate of BRL 30 bn

Source: Ministry of Finance

Business Environment Improvement

Modernize Labor Legislation (PL 6.787/2016, PLC 30/2015)

- Collective Agreements will prevail over Law Provisions (relative to 13 points)
- Temporary work contracts maximum period will go from 3 to 8 months
- Improvements in the Job Protection Program (PPE), renamed Job Insurance Program (PSE)
  - New admission criteria
  - Maximum annual cost
  - Fines and punitive measures in case of fraud and noncompliance with the program rules

Tax Reform: Simplify Tax System

- Expected to be submitted to Congress still in 2017
- Focus: PIS and Cofins (federal) , ICMS (state)
- Announced measures in the subject includes a series of system to reduce red-tape costs

Agenda BC+: lower neutral rate and higher MoP Effectiveness

- The main goal is to pursue a more efficient financial system, with more free market credit, contributing to increase the power of monetary policy.

- Based on four Pillars:

I. Increase financial citizenship

II. Increase financial system efficiency

III. Improve legal framework

IV. Reduce cost of credit

Directed Credit, Quasi-Fiscal Impulses and Long Term Rates

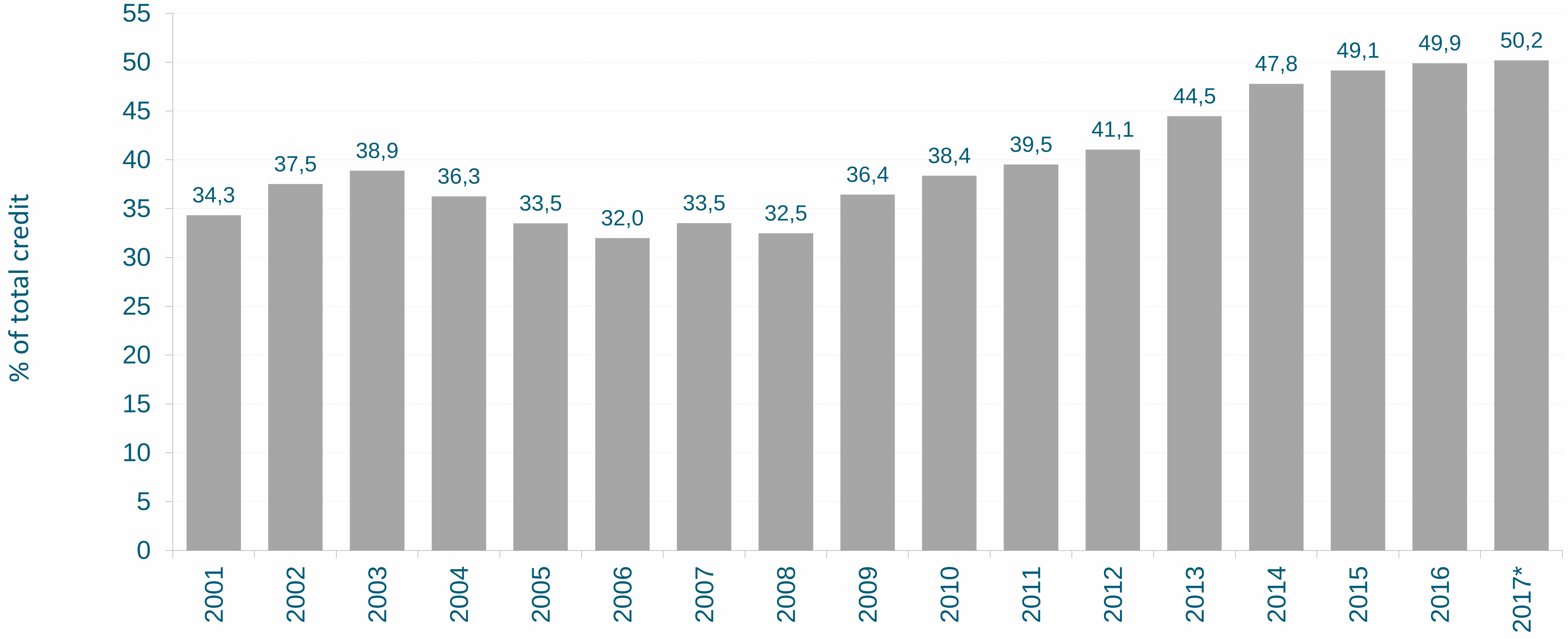
- New economic policy involved a significant decrease in expansionary quasi-fiscal impulses

- From the monetary policy standpoint, a more efficient financial system, with more free market credit, contributes to increase the power of monetary policy.

- **Structural measures (Agenda BC+)** aim to reach a sustainable reduction in overall cost of credit, increasing economic efficiency and productivity, thereby helping monetary policy effectiveness

- **New methodology for TLP** (parameter for the remuneration system of directed credit) aligned with market rates favors monetary policy effectiveness.

Earmarked Credit



Source: BCB

new methodology since Mar 07

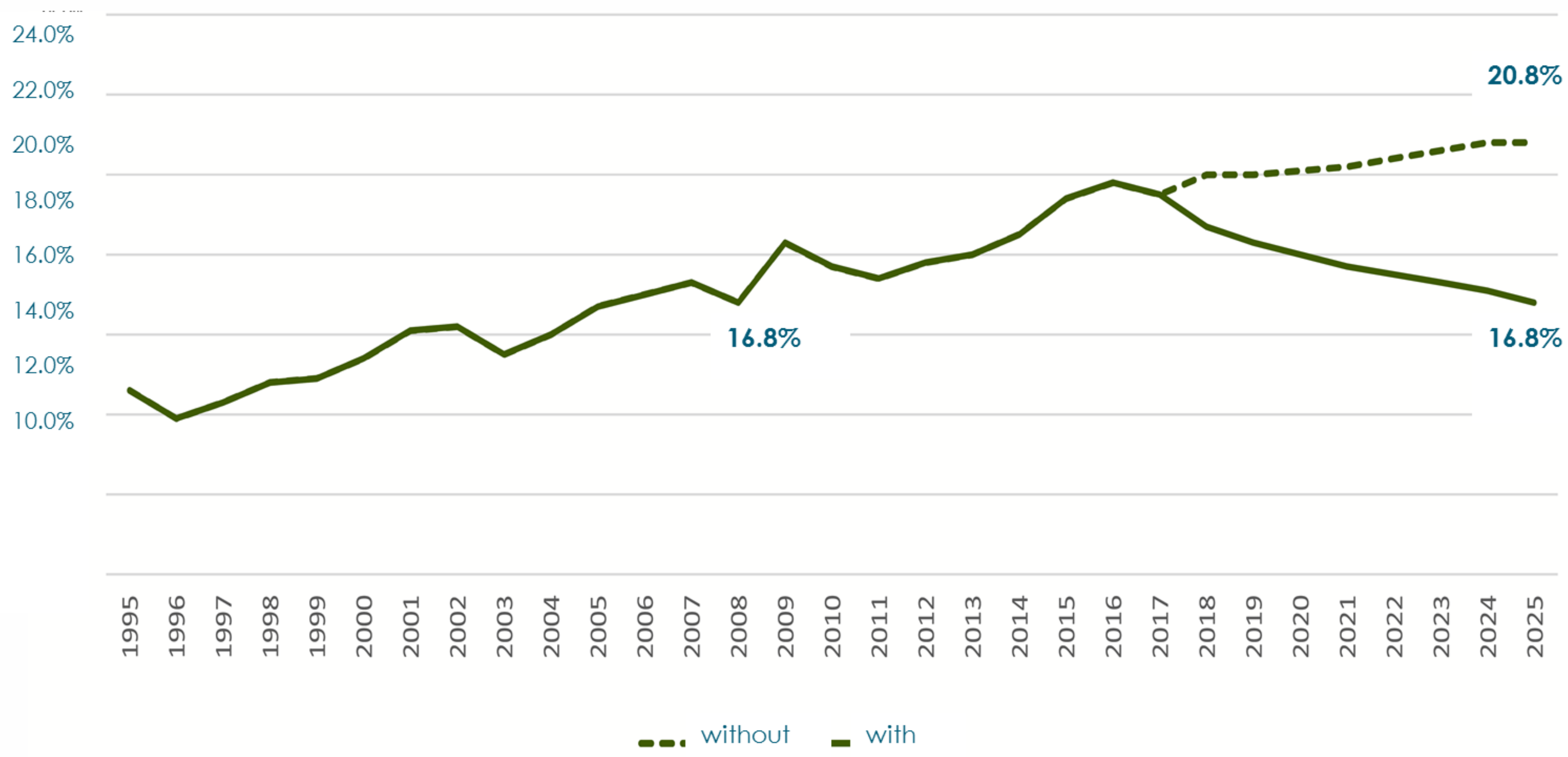
*Feb/17

Structural Fiscal Reform Agenda and Monetary Policy Effectiveness

- Persistent growth in expenditures caused a **fiscal deterioration that eroded confidence.**
- **Structural Fiscal Reform Agenda is critical** to bring fiscal equilibrium back, assuring public debt sustainability through a recovery in primary surpluses' horizon;
- **Intertemporal consistency in fiscal policy is critical for monetary policy effectiveness,** definitively removing uncertainty for longer horizons.
- **Spending Ceiling -** *Constitutional Amendment was approved in October 2016.*
- **Social Security Reform** is under sound debate in the society, and in advanced consideration in the Chamber, with expected examination in the floor by mid-May.

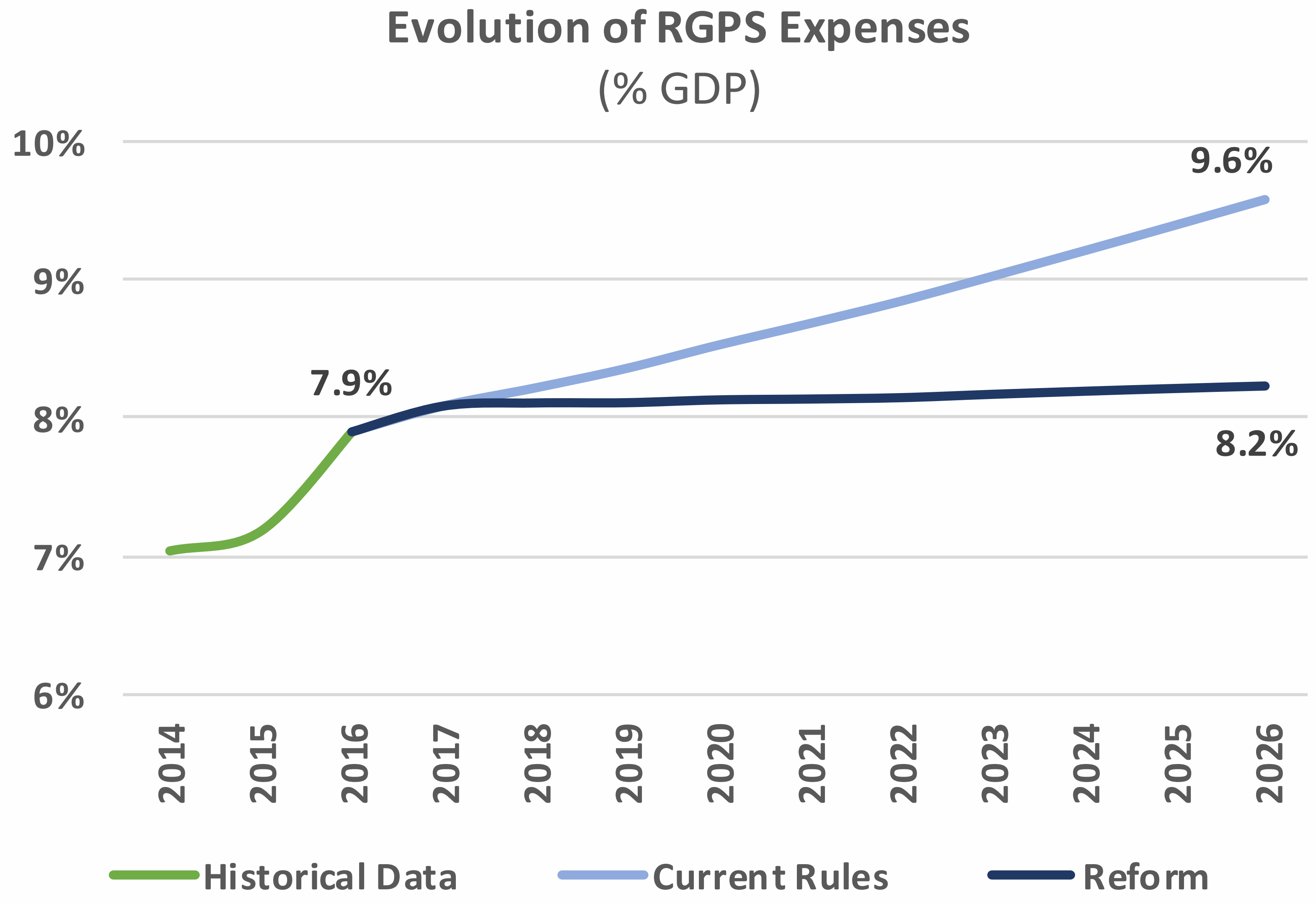
Spending Cap will anchor fiscal policy opening room for primary surpluses

Projection of Primary Expenditures with and without Expenditures Cap (% GDP)



Source: National Treasury Secretariat

Social Security Reform - Key Features and Positive Impacts



Source: National Treasury Secretariat

Outlook for the Brazilian Economy: Conclusions (I)

- **Positive outlook for global economic activity, but relevant global uncertainty and risks for EME** (faster tightening in US, protectionism, Europe´s politics, Protectionism and global growth, and Outlook for Chinese economy)

- **Brazil is resilient to external volatility and risks.** Sound current account financing through FDI; Low overall exposure to forex liabilities including corporates; diversified trade ties (global trader) and financial system with solid capital structure and limited leverage.

- Monetary Policy easing, microeconomic reform agenda, and structural sound growth in agriculture favor a **gradual growth recovery along 2017**.

- **Real and nominal interest rates are falling in Brazil.** The policy rate (Selic) fell during the past few months and it is expected to fall further. The real interest rate have also receded.

Outlook for the Brazilian Economy: Conclusions (II)

- **Favorable inflation dynamics, with widespread disinflation**, lower persistence and expectations well anchored for longer horizons

- Consolidation of a disinflation for inflation components that are most sensitive to the economic cycle and to monetary policy justified **a moderate intensification of the monetary easing process. The Committee judged the pace of 100bps adequate**.

- **Structural Fiscal Reform Agenda is critical to assure public debt sustainability, definitively removing uncertainty for longer horizons.** Spending Ceiling was approved in Oct/16, and the Social Security Reform is under advanced consideration in Congress.

Thank You!

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