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BRAZIL BULLETIN INTERVIEW: Vladimir do Vale, Chief Strategist Banco Credit Agricole –"As soon as the government finds a new way to tax inflows, the banks find a new way to get around it."-- Despite the good times enjoyed by most Brazilians in recent months, the country faces new inflationary pressures and more interest rate hikes in 2011. Such problems will hit the radar "sooner rather than later," according to Vladimir do Vale, Chief Strategist for Banco Credit Agricole in São Paulo. Vale discussed the 2011 outlook at a recent conference. Excerpts follow:

- On industrial capacity: "Utilization of industrial capacity is once again high. That means any increase in demand turns almost automatically into a new source of inflationary pressure. This is why analysts are consistently increasing their 2011 inflation outlook, which is now well above 5.0%."
- On interest rates: "Even at rates of over 10%, the Selic base rate is expansionist. The market is beginning to say the Central Bank is behind the curve on inflation."
- On the Rousseff administration and fiscal policy: "No one really knows Dilma Rousseff's views on fiscal tightening. From what little she has said, she seems to think that it's only necessary to hold the debt-to-GDP ratio steady, not pull it down."
- On the trend for the Brazilian Real: "Higher interest rates will make Brazilian investments even more attractive than they already are. That means the trend toward a stronger Real will continue. The strong Real, in turn, will continue to hurt exports."
- On tax measures and the Brazilian Real: "Government tax measures designed to curb the appreciation of the Brazilian currency don't work very well. The Brazilian financial industry is sophisticated and well integrated internationally. As soon as the government finds a new way to tax inflows, the banks find a new way to get around it."
- On economic growth: "On the positive side, Chinese growth and demand remain strong. That means high international commodities prices will continue. Brazil could enjoy average annual growth of 4.5% or so for the next ten years."

More than 500 dead as heavy rains, landslides pummel Rio de Janeiro. In what some commentators are calling the worst natural disaster in Brazil's history, heavy rains and landslides hit Rio de Janeiro and its mountain suburbs last week, leaving more than 500 dead. Worst hit were the resort cities of Nova Friburgo and Teresopolis and the former imperial city of Petropolis. A week of heavy rains led to landslides and flooding throughout the region, leaving at least 500 dead, the state's Civil Defense Department said. In addition, another 5,000 lost homes while thousands more were forced to flee their rain-soaked neighborhoods. President Dilma Rousseff and Rio de Janerio Governor Sergio Cabral toured the region by helicopter. The president made R$780 million in emergency funds available to the state and to affected municipalities. But officials were also frank in admitting that much of the problem was due to decades of poor zoning practices and lax enforcement of building codes. Rio de Janeiro Environmental Affairs Secretary Carlos Minc said the chief problem was what he called "criminal occupation of hillside slums." Rousseff admitted that "housing in risk areas has become the norm, rather than the exception…This is not just a natural disaster, but also a problem of irregular occupation of the soil." Rousseff and Cabral promised to study plans for development of better zoning and enforcement practices in the region. São Paulo state also reported heavy rains and flooding, with 13 dead from the storms.

Retail sales show unexpected growth in November, IBGE says. Retail sales showed unexpectedly robust growth in November, despite weakness in supermarket revenues, the Brazilian Census Bureau (IBGE) said last week. Retail sales jumped 1.1% in November against October and 9.9% against November of 2009. Office equipment led the advance at more than 10% while textiles showed a decline of 3.6%. Supermarket sales dropped 0.1% against October, mainly because of high prices for perishables. November performance bested that of October, when retail sales grew only 0.5%, month-on-month.

Petrobras report shows oil and gas reserves advancing 7.5% in 2010. Proven reserves of crude oil and natural gas controlled by state-run energy company Petrobras rose 7.5% in 2010 to the equivalent of 15.99 billion barrels-of-oil, the company said last week. Petrobras incorporated only 1.07 billion barrels of oil from its new sub-salt region into the proven reserve figure. The company is likely to incorporate more sub-salt oil into proven reserves by the end of 2011. Petrobras produced 869 million barrels of oil-equivalent in 2010, the report said. That figure was replenished, plus more, by the new sub-salt reserve as well as increased proven reserves in other regions, especially the Campos Basin off the coast of Rio de Janeiro. At current rates of extraction, Brazil has enough oil for the next 14.7 years, the report said. The Petrobras report cited proven reserves under criteria used by Brazil's National Petroleum Agency (ANP). Under international criteria maintained by the U.S. Securities and Exchange Commission (SEC), Brazil's proven reserves rose in 2010 by 5% to 12.76 billion barrels of oil-equivalent.

Anfavea raises 2011 forecast for auto sales, predicting a new record at 3.69 million. Brazil's National Motor Vehicle Manufacturers Association (Anfavea) last week raised its forecast for 2011 auto sales to 3.69 million, which would constitute a new record. Sales are likely to rise as Brazil's economy builds on its 2010 boom, based on job opportunities, rising incomes and ample availability of credit. Motor vehicle production in 2011 will also set a record at 3.68 million, Anfavea said. Exports will reach $13.1 billion, not quite enough to surpass the standing record of $13.9 billion set in 2008. Actual 2010 sales were 3.5 million, up 11.9% from 2009. Production in 2010 reached 3.64 million, up 14.3% from the previous year. Exports in 2010 were $12.86 billion, a stunning rise of 55% from 2009.

Study shows Brazil emerging as world's number four economy by 2050. Brazil will pass France, Britain and even Germany and Japan to become the world's fourth biggest economy by 2050, according to a study last week by PriceWaterhouseCoopers. By the middle of the century, Brazil will be surpassed only by China, India and the United States. Brazil's progress from a current ranking of ninth to a new ranking of fourth depends on continued heavy investments in education and infrastructure, according to the study. The study is based on average annual growth for the Brazilian economy of 4.4%. On a per capita basis, however, Brazilians will continue struggling. Currently, Brazil's per capita income is equal to only 22% of the average U.S. resident, according to the study. In 2050, Brazil's per capital income will hit 50% of the U.S. average.

Investment News: Japan's **Mitsui & Co.** last week announced the purchase of a 44% stake in Brazilian grain and oilseeds giant Multigrain SA for $225 million. Mitsui already owned 44% of Multigrain and aims to eventually make the company into a wholly owned subsidiary. Multigrain controls farmland, port facilities and flour mills in Brazil.

Company News: U.S.-based **Global Payments Inc**. last week announced it will establish its own credit- and debt-card processing service in Brazil this year to compete with market behemoths Redecard and Cielo. The company said it does not plan any acquisitions in Brazil. Global Payment's aim is to tap into a domestic market for credit card services that has been growing at better than 10% per year for the last decade.

Indicators: Domestic **air traffic** in Brazil grew by an astonishing 23.5% in 2010 against the previous year as airlines added to their fleets and won new passengers with steep discounts, the Civil Aviation Authority (Anac) said last week. Air traffic hit 70.2 billion passenger-kilometers in 2010. TAM and GOL continued the market leaders, with about 80% of the total market. But upstarts such as Azul, WebJet and Ocean Air are likely to make inroads in 2011. *** **Primary aluminum output** rose by a bare 0.1% in 2010 from the previous year to 1.536 million metric tons, the Brazilian Aluminum Association (Abal) said last week. Growth for the industry was hobbled by closing down of the Novelis plant in Aratu, Bahia.

Other News: The Brazilian government last week authorized the country's **Sovereign Wealth Fund** to operate in the domestic foreign exchange market as well as the foreign exchange derivatives market. The Central Bank and the Federal Treasury are already authorized to operate in foreign exchange markets. The frank intention of the new rule is to create another source for government intervention in foreign exchange, with a view toward preventing further appreciation of the Brazilian Real against the U.S. dollar. The strong Real has hurt Brazilian exports. The Real has gained more than 30% against the dollar since 2009.

Brazilian Calendar for Week of January 17:

- **Wednesday,** January 19, Brazilian Central Bank Monetary Policy Committee (Copom) meeting

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R$1.68 = $1.00