Brazil Bulletin
an exclusive member service of the Brazil-U.S. Business Council

Brazil-U.S. Business Council, Brazil Bulletin, Vol. XXI, No. 19
May 9, 2011

BRAZIL BULLETIN INTERVIEW: Deputy Brazilian Treasury Secretary Paulo Valle and Chief Brazilian Treasury Strategist Otavio Medeiros: "We want the private sector to take an increased role in financing." The Brazilian Treasury is in the enviable position of being able to ratchet down both lending and borrowing operations this year as the domestic economic recovery hits full stride, two top Treasury officials told investors in a recent conference call. Excerpts from the call with Deputy Treasury Secretary Paulo Valle and Chief Treasury Strategist Otavio Medeiros follow:

- Medeiros: "The improving economy means Brazil's primary budget surplus rose from 2.1% of GDP in 2009 to 2.8% in 2010. In 2011, we will easily reach the goal of 3.0%. With that, we will be able to reduce the net debt-to-GDP ratio by two percentage points per year for at least the next few years. The debt-to-GDP ratio ended at 40.4% in 2010. We could go as low as 31% by the end of President Rousseff's term in 2014."
- Valle: "When it comes to meeting overseas debt service payments, we are in an unusually comfortable position. We have already purchased 75% of the dollars we need for 2011 and 2012. We will only need to conduct overseas operations because of our commitment to maintaining liquidity for benchmark bond issues."
- Medeiros: "It's true that the current account deficit will rise to about $70 billion in 2011 but we expect foreign direct investment at about $50 billion to cover most of that and portfolio investment to cover the rest. With foreign reserves at $300 billion, we don't see any risks to the current account."
- Valle: "The Brazilian National Development Bank (BNDES) will continue as an important source of lending in 2011, especially in the area of long-term infrastructure projects, but we want the private sector to take an increasing role in financing."
- Medeiros: "What Brazil has done to control short-term investment inflows is not different from what other countries have done. We are guaranteeing less, not more, foreign exchange volatility. From the investor viewpoint, it's better to have a stable currency than a volatile one. Imagine if the Real went to R$1.50 to the dollar one year and then R$2.20 the next."

Inflation breaks through ceiling of target range, may exceed 7.0%. Brazil's official IPCA inflation rate broke through the ceiling of the country's target range for 2011 last week, posting a 12-month rate of 6.51%. Under Brazil's inflation-targeting program, the country is committed to inflation this year of 4.5%, but with two percentage points of leeway. That makes 6.5% the outer limit of the range. Inflation has been on the march because of soaring fuel and food prices. According to economists at Barclays Capital, inflation is going to get worse before it gets better. Barclays is predicting a peak for annual inflation of 7.7% in August. April monthly inflation, as outlined last week by the Brazilian Census Bureau (IBGE), weighed in at 0.77%, down very slightly from 0.79% in March. On the positive side, food prices rose only 0.58% and may decelerate even more in the coming months as the grain and oilseeds harvest comes on stream. Finance Minister Guido Mantega said monthly rates have already peaked. He predicted May monthly inflation no higher than 0.50%.

Auto sales still strong year-on-year but decline in April from previous month. Brazilian motor vehicle sales in April reached 289,189, up 4.1% from the same month a year ago but down 5.5% from March, the National Motor Vehicle Manufacturers Association (Anfavea) said last week. Sales decline month-on-month because of new credit restrictions put in place by Brazil's government earlier this year. Higher taxes on consumer credit are designed to help fight down inflation, now running at 6.5% per year. Anfavea said the percentage of car sales attached to financing declined in April to 62% from 66% in April of 2010. "The credit crunch is beginning to have its effect," said Anfavea President Cledorvino Belini. Auto exports in April were 42% higher than in April of 2010 as the global economic recovery gathered steam. Production in April was 280,128 vehicles, up 1.9% from April of 2010.

Industrial output continues advance in March, but could spell inflation. Brazilian industrial production increased 0.5% in March over February, despite Carnival holidays that occurred in March this year, the Brazilian Census Bureau (IBGE) said last week. It was the third straight monthly advance in industrial output. Production was led by a 10.1% gain for electronics goods. Capital goods expanded 1.8%. Thirteen of the 27 segments surveyed showed month-on-month gains. On a 12-month basis, industrial output grew 6.8%. But the continued rise of industrial output led many economists to predict continued pressure on inflation. Rising inflation could bring a new round of interest rate hikes.

Investment News: U.S. food and beverage company **Kraft Foods** last week announced additional investments in its Brazilian operations of $200 million over the next two years. Investments will be aimed at expanding the company's presence in the North and Northeast. Kraft sells 35 separate brands in Brazil, worth $2 billion in annual revenues. *** The Brazilian subsidiary of **Suzuki** last week announced investments of R$100 million to build the Japanese company's first assembly line in Brazil. The plant will be located in Itumbiara, Goias and will open for business at the end of 2012. The Itumbiara assembly line will produce 7,000 Suzuki Jinny SUV models per year. *** The Brazilian subsidiary of U.S. retail giant **Wal-Mart** last week announced R$1.2 billion in investments for 2011. The company has averaged R$1.2 billion in annual investments every year since 2006. This year, the company will open 80 new stores and will upgrade logistics and technology. Wal-Mart already has 483 outlets in Brazil under nine different brand names. *** Brazilian steel giant **Gerdau** last week announced a $347 million investment plan for the company's U.S. properties through 2014. Gerdau will boost output in the U.S. by 400,000 tons, with investments in holdings in Arkansas, Michigan and Minnesota. Gerdau said it expects American steel demand to rise with the recovery of the auto industry.

Company News: The Board of Directors of mining giant **Vale** last week approved a major expansion of the Samarco iron ore project the company owns jointly with **BHP Billiton.** The partners will invest an additional $3 billion to build a fourth iron ore pellet plant with annual capacity of 8.3 million metric tons, bringing total capacity to 30.5 million. The investment also involves port improvements at the Ponta Ubu site in Espirito Santo and expansion of an ore pipeline. *** Brazil's largest private bank, **Itau,** last week announced first quarter profits of R$3.53 billion, up from R$3.23 billion for the same quarter of 2010. The company's lending portfolio expanded to R$344.8 billion from R$282.9 billion the previous year. Provisioning against bad loans increased to R$4.38 billion from R$3.8 billion in the first quarter of 2010. *** Mining giant **Vale** last week reported record first quarter profits of $6.83 billion, triple the company's first-quarter 2010 performance. Revenues doubled from 2010 to $13.2 billion. Vale gained from both higher prices and an increase in output and exports. International demand, especially from China, staged a major rebound in the first quarter, the company said.

Indicators: Brazil rolled up an unexpectedly hefty April foreign **trade surplus** of $1.86 billion, up from $1.55 billion in March and $1.28 billion in April a year ago, the Trade and

Development Ministry said last week. Exports have risen faster than imports so far this year because of higher global commodities prices. Brazil's year-to-date surplus through April was $5.03 billion, more than double the four-month surplus of $2.16 billion for the same period of 2010. *** Brazilian **crude oil output** grew 2.2% in April from the previous month and 1.0% from April of 2010, the National Petroleum Authority (ANP) said last week. Output reached 2.082 million barrels per day as idle offshore platforms came back on stream following maintenance. State-run energy giant Petrobras accounted for fully 93% of production.

Other News: Brazil's Federal Accounting Office (TCU) last week announced a broad review of **toll-road contracts** signed before 2007. The TCU said pre-2007 contracts were paying concession-holders at real profit rates of 17% to 24%. The office said concession-holders should be held to the post-2007 standard of about 9%. Industry representatives said they would fight any effort to overturn existing contracts.

Brazilian Calendar for Week of May 9:

- **Monday, May 9 -** International Communications Leadership Congress, Hotel Transamerica, São Paulo
- **Tuesday, May 10** - The Brazilian Association for Real Estate and Tourism Development Meeting, Fortaleza, Ceara
- **Tuesday, May 10 -** Banco do Brasil release of quarterly earnings, Brasília
- **Tuesday, May 10** - Fourth Annual Emerging Markets Forum, Itau Cultural Institute, São Paulo
- **Thursday, May 12 -** Inside Market Data Conference, Sheraton WTC Hotel, São Paulo
- **Thursday, May 12 -** Brazilian Census Bureau (IBGE) release of monthly retail sales data, Rio de Janeiro
- **Friday, May 13 -** Petrobras release of quarterly earnings data, Rio de Janeiro

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R$1.61 = $1.00