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BRAZIL BULLETIN INTERVIEW: Luciano Coutinho, President of the Brazilian National Development Bank –"The challenge is to control inflation without provoking recession." Brazil's government-run National Development Bank wants to gradually withdraw from the lending business, according to BNDES President Luciano Coutinho at a recent investment seminar in São Paulo. During the conference, Coutinho shared his views with reporters accredited to the BNDES. Excerpts follow:

- On lending and the private sector: "An indicator of success for the BNDES this year would be a reduction in lending volume because that would mean an increase in scope for private lending. We want to reduce the 'crowding in' effect by the bank. But we can't promote a radical reduction of the BNDES' presence in the market. If we hit this year's target of R$140 billion to R$145 billion in lending that will represent roughly stable lending volume versus 2010, which is what we are aiming for."
- On investments and foreign exchange: "Productive investments from overseas are welcome and will continue to be welcome. What we are worried about are short-term speculative investments. The government already has the instruments it needs to mitigate the impact on the foreign exchange rate due to the increase in foreign investments. The government will use these instruments if necessary. However, it will not use these instruments to restrict productive investments."
- On inflation and growth: "Brazil's government has a commitment to keep inflation low in the medium and long term. Stability is fundamental to the investment climate. The challenge is to control inflation without provoking recession. We need a coordinated, well calibrated response. We need to mitigate aggregate demand while absorbing shocks from the rise in global commodities prices. We also need to maintain the investments that are essential to our long-term growth."
- On investment and growth: "Brazil's investment rate will rise this year. We expect an increase in investments of 8% to 10%, while GDP rises about 4.0%."
- On the economic policy team: "There is no truth to the idea of conflict within the economic policy team. The BNDES, the Central Bank and the Finance Ministry are all working well together. We're in tune."

Brazil posts modest first quarter growth of 4.2% as domestic consumption slows. Higher interest rates and curbs on consumer credit may already be having the desired effect of cooling Brazil's once overheated economy, the Brazilian Census Bureau (IBGE) said last week. Gross domestic product expanded by 1.3% over the fourth quarter of 2010 and 4.2% over the first quarter of last year. Overall growth was much slower than in 2010, when the economy expanded by a sizzling 7.5%. Rapid growth last year was led by consumer demand, which brought a worrisome hike in inflation. Brazil closed out 2010 with annual inflation of 5.9%, up sharply from 3.1% the previous year. Inflation is now running at an even higher rate of 6.5%, which may prompt a new round of interest rate hikes and credit curbs. In absolute terms, Brazilian GDP reached R$940 billion in the first quarter. The investment rate was up slightly at 18.4% of GDP from 18.2% in the first quarter of 2010. Finance Minister Guido Mantega said the government was sticking with its forecast of 4.5% for overall growth this year.

U.S. House Appropriations Committee vetoes key element of U.S.-Brazil cotton deal. The U.S. House of Representatives Appropriations Committee last week vetoed a key element of a 2010 accord between the United States and Brazil designed to avoid some $829 million in trade retaliation against U.S. businesses. The committee voted to eliminate an annual U.S. payment of $147 million to Brazil's cotton industry beginning in fiscal 2012. The payments were being made following a World Trade Organization ruling against U.S. subsidies to cotton growers. In 2010, Brazil agreed to accept the payments, along with other concessions, in exchange for holding off on trade retaliation measures authorized under the WTO ruling. The $147 million can still be restored by full House action.

Government posts huge April surplus, all but guarantees 2011 target. Brazil's public sector posted a whopping primary budget surplus of R$18.05 billion in April, up sharply from R$13.6 billion in March. The 12-month surplus was R$121.9 billion, or 3.14% of gross domestic product. The 12-month figure was above the government's 2011 calendar year goal of R$117.9 billion for the surplus. With continued heavy tax collections likely in the coming months, and firm spending controls in place, Brazil was all but assured of meeting the annual target, government economists said. April was aided by huge tax revenues of R$85.2 billion, up from R$70.9 billion in March. The surplus, however, does not include service payments on debt. With such payments factored in, April saw a nominal deficit of R$1.6 billion for a 12-month nominal deficit of R$94.3 billion, or 2.47% of GDP.

Lending volume continues rise despite government measures to curb credit. Brazilian lending volume continued to expand in April despite government efforts to fight down inflation by reducing consumer credit, according to central bank figures last week. Total lending volume as of April was R$1.78 trillion, up 1.3% from March and 21.0% from April of 2010. Lending expanded faster in April than in March despite government efforts to curb credit. March saw a month-on-month expansion in lending volume of 1.0% and a year-on-year expansion of 20.7%. Credit is still expanding faster than in 2010, when total lending volume grew 20.1%. Earlier this year, Brazil's government began a campaign to pull down inflation by curbing credit expansion, especially for consumers. To date, government measures have included higher reserve requirements for banks, a hike in financial operations taxes over many forms of consumer credit and higher interest rates. Brazil's Selic base rate is a towering 12.0%, up from 10.75% at the end of 2010. Inflation is running at a worrisome 6.5%, up from 5.9% in

2010. Meanwhile, average interest rates continued to rise, in line with government efforts to discourage consumer indebtedness with higher borrowing costs. The average annual interest rate on all loans hit 39.8% in April, up from 39.0% in March. The average annual interest charge for consumer credit rose to a punishing 46.8% in April, up sharply from 44.2% in March. Arrears rose to 4.9% in April from 4.7% in March.

Report says Brazil to see less growth, more inflation than expected in 2011. Brazil will see less growth and more inflation in 2011 than previously expected, the government said in its bi-monthly economic report last week. The Finance Ministry report reduced the government's forecast for gross domestic product expansion in 2011 to 4.5% from a previous forecast of 5.0%. Growth in 2010 was a stunning 7.5%. But Brazil's 2010 economic performance came at the price of rising inflation, with price pressures persisting into 2011. The report forecast 2011 inflation of 5.6%, up from the previous forecast of 5.0%. Inflation in 2010 was a worrisome 5.9% and has since risen, on a 12-month basis, to 6.5%. The recent rise in the 12-month inflation rate has led the government to take a number of steps to slow down the economy. These include curbs on consumer credit, higher interest rates and cuts in federal spending. The government now expects consumer spending in 2011 to rise just 5.9%, down from the previous forecast of 6.4%. Consumer spending rose by a robust 10.3% in 2010. But Brazil's investment rate will also slow down, the report said. The government is now forecasting an investment rate equal to 19.5% of gross domestic product, down from a previous forecast of 20.4%. Brazil's 2010 investment rate was 18.5% of GDP.

Investment News: State-run **Banco do Brasil** last week beat out three other rivals to win the government concession to operate postal banking services. Banco do Brasil paid R$3.15 billion at auction for the right to establish banking operations at 6,000 post offices throughout the country. Banco do Brasil will hold the concession through 2017.

Company News: **Royal Dutch Shell** and **Cosan Industria e Comercio** last week formalized creation of their new Brazilian ethanol joint venture, called **Raizen**. The company immediately became the world's biggest sugarcane and ethanol concern. The company expects to produce two billion liters per year of ethanol made from Brazilian cane. Cosan Chairman Rubens Ometto will double as Raizen chairman.

Indicators: Electric power demand in April increased by an extremely modest 2.4% against the same month in 2010, as residential consumption remained nearly flat and Brazil's economic expansion slowed, the government's Energy Research Corp. (EPE) said. Energy use reached 35,835 megawatt-hours in April. Industrial use rose 2.9% while residential consumption was up a bare 0.9%. Energy use for the first four months of 2011 was up 4.1% at 142,744 megawatt-hours, EPE said. *** **Industrial production** slid in April by 2.1% against March and 1.3% against April of 2010 as manufacturers wrestled with a flood of cheap imports and consistently high domestic interest rates, the Brazilian Census Bureau (IBGE) said last week. Durable goods output slumped 10%, while capital goods dropped 5.4%. *** Brazil's **foreign trade surplus** soared in May to $3.5 billion from $1.9 billion in April on rising international commodities prices, the Trade and

Development Ministry said last week. The year-to-date surplus was $8.6 billion, up from $5.6 billion for the same period a year earlier.

Other News: Brazil's government last week announced that it will partially privatize operations at **three major airports** ahead of the 2014 World Soccer Cup. At a date to be set for later this year, the government will auction majority stakes for concessions to Guarulhos Airport in São Paulo, Viracopos in Campinas and Juscelino Kubitschek in Brasília. The government's airport authority, Infraero, will retain a 49% stake in all three airports. More airport concessions are likely to be auctioned next year.

Brazilian Calendar for Week of May 30:

- **Monday, June 6 -** Seminar on Nanotechnology and New Industrial Materials, Milenium Convention Center, São Paulo
- **Monday, June 6 -** Annual Industry Association Seminar on Investor Relations and Corporate Governance, Hotel Renaissance, São Paulo
- **Monday, June 6 -** National Motor Vehicle Manufacturers Association (Anfavea) release of monthly production, sales and export figures, Sofitel Hotel, São Paulo
- **Monday, June 6 -** Venezuelan President Hugo Chavez visit to Brasília
- **Monday, June 6 -** Annual Brazilian Ethanol Summit, Grand Hyatt Hotel, São Paulo
- **Tuesday, June 7 -** Brazilian Census Bureau (IBGE) release of IPCA inflation data, Rio de Janeiro
- **Wednesday, June 8 -** Brazilian Central Bank Monetary Policy Committee (Copom) review of Selic base interest rate, Brasília
- **Friday, June 10 -** National Power Authority (Aneel) auction of transmission line concessions, Brasília
- **Friday, June 10 -** Brazilian Census Bureau (IBGE) release of monthly retail data, Rio de Janeiro

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R$1.58 = $1.00