



# *Brazilian Economy Overview:*

## *A New Development Cycle*

*Guido Mantega  
Minister of Finance  
April 2008*



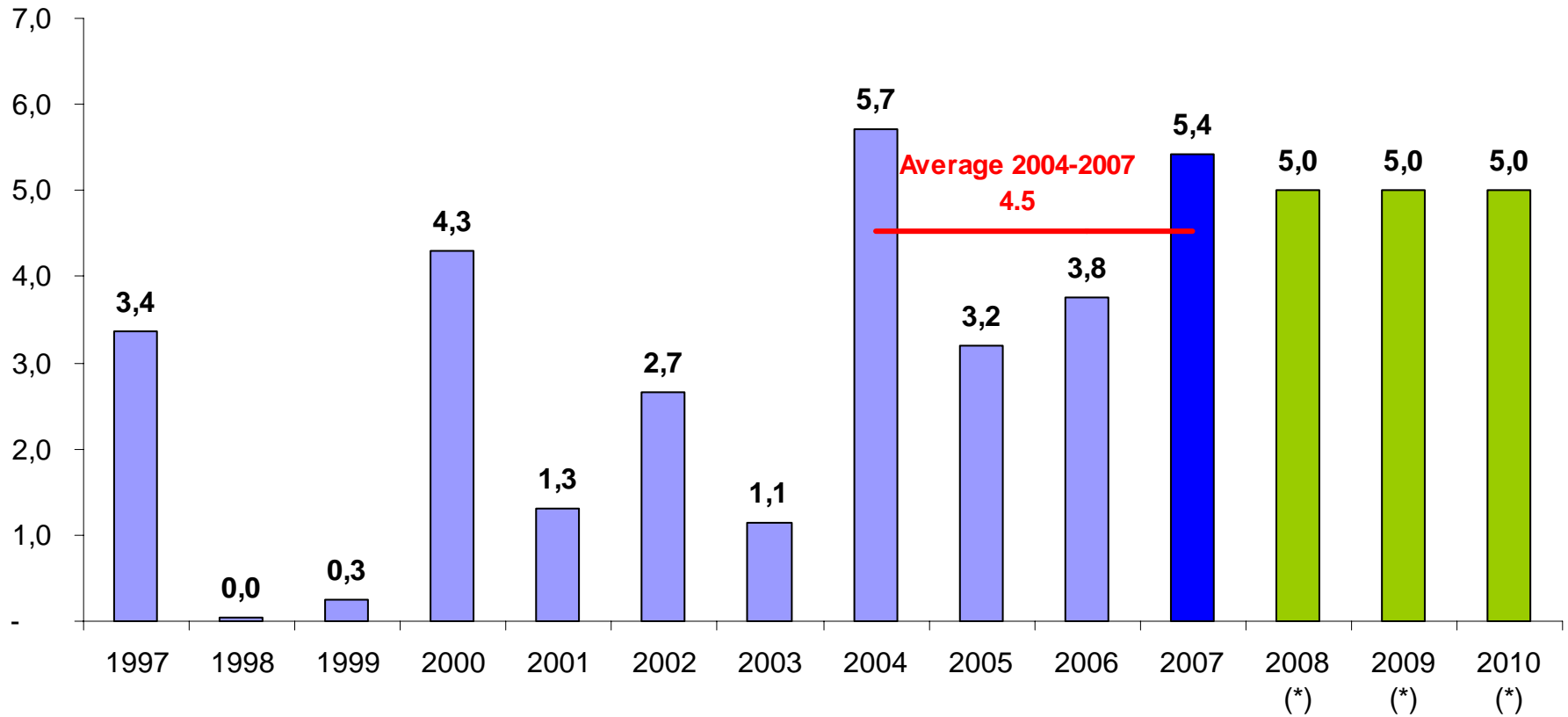
## SUSTAINABLE GROWTH

- **A sustainable growth process is under way.**
- **A new cycle of economic growth with:**
  - Higher rates of growth
    - GDP growth: 24 consecutive quarters
    - Consumption growth: 17 consecutive quarters
    - Investment growth: 16 consecutive quarters
  - Based on foreign trade and mass consumption
  - Fiscal Commitment
  - Inflation under control



# GDP GROWTH

(annual rate – %)



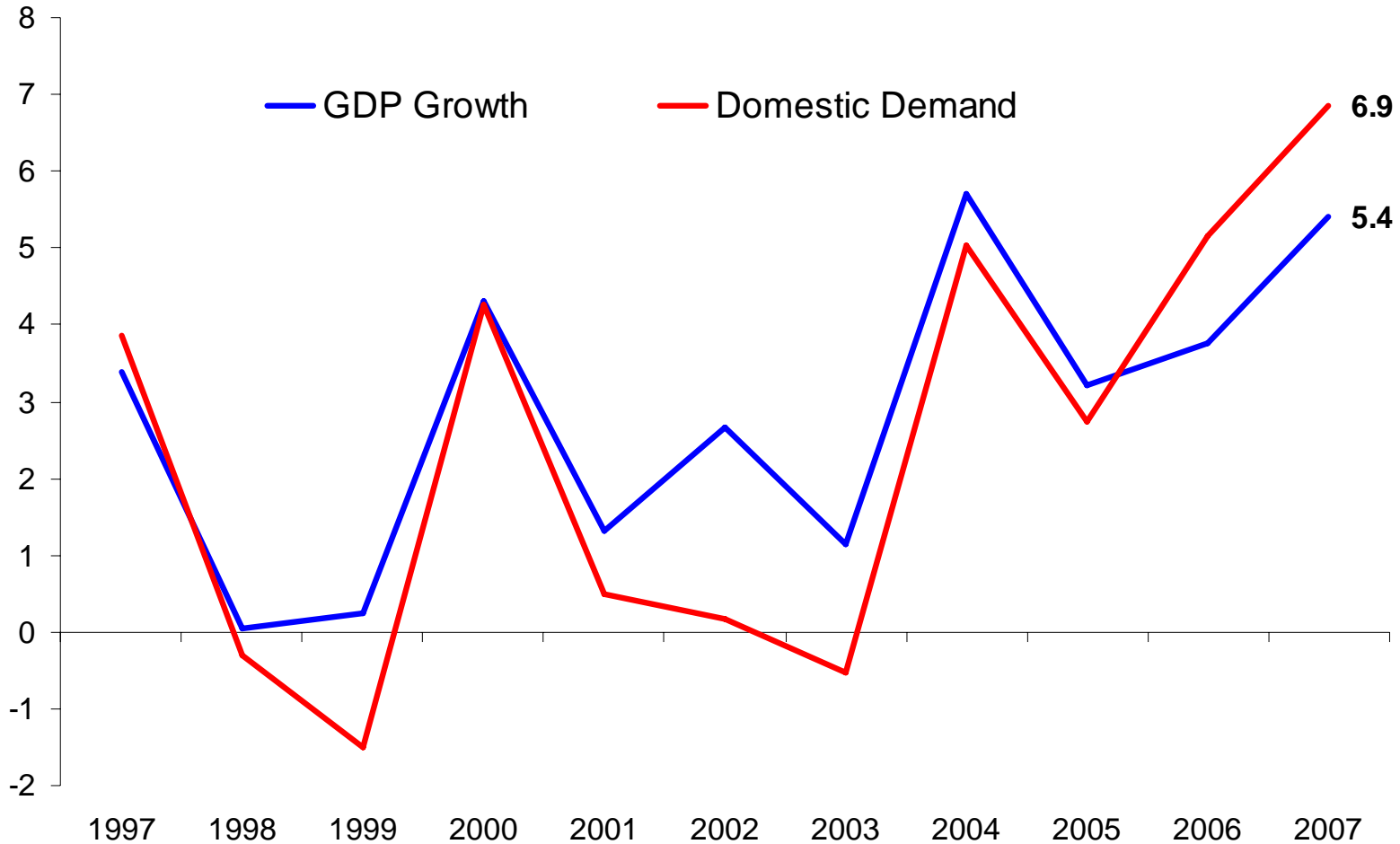
\*/ Government projections (PPA 2008-2011)

Source: IBGE.

Prepared by: MF/SPE.



# CONTRIBUTION OF DOMESTIC DEMAND TO GDP GROWTH (%)



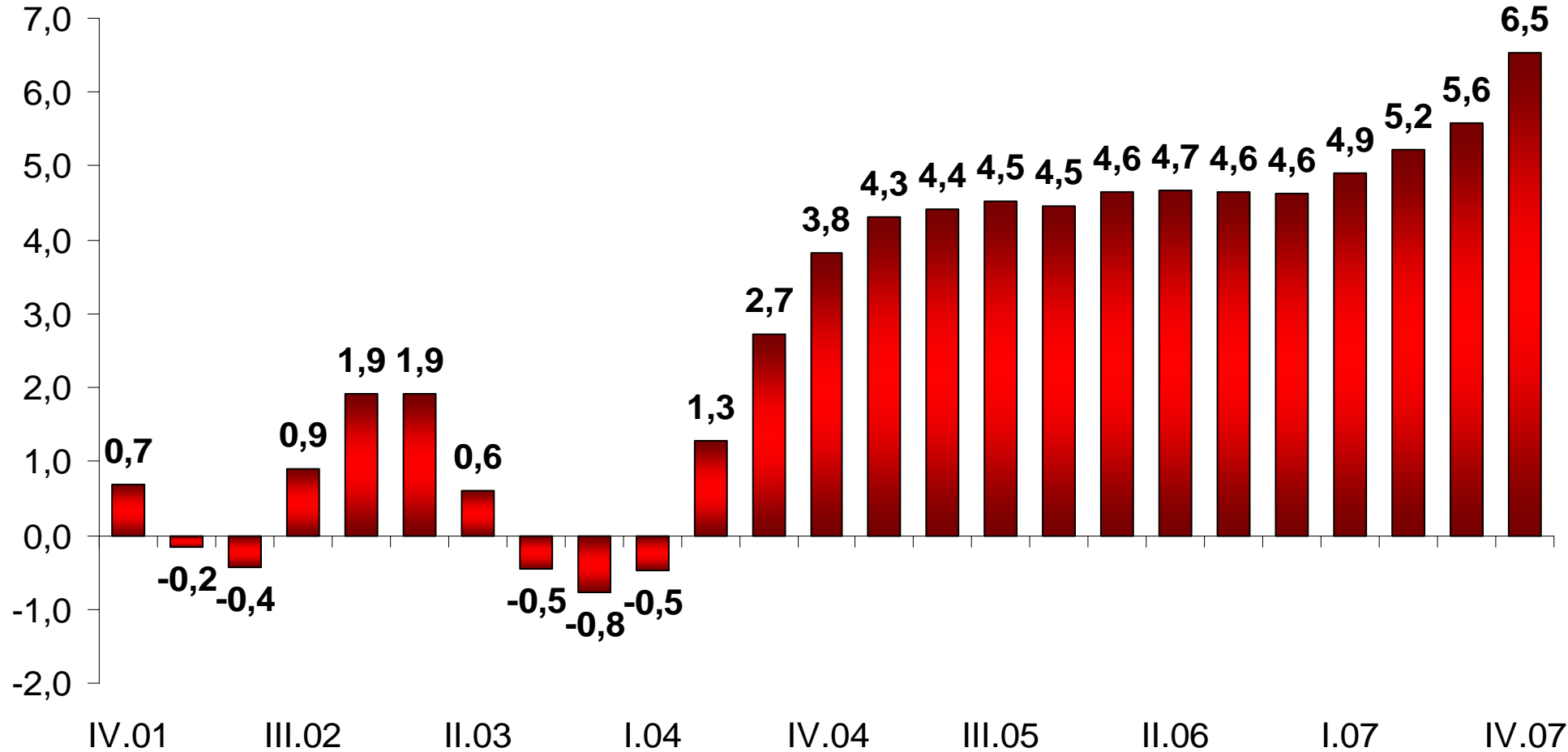
Source: IBGE.

Elaborated by: MF/SPE.



# HOUSEHOLD CONSUMPTION

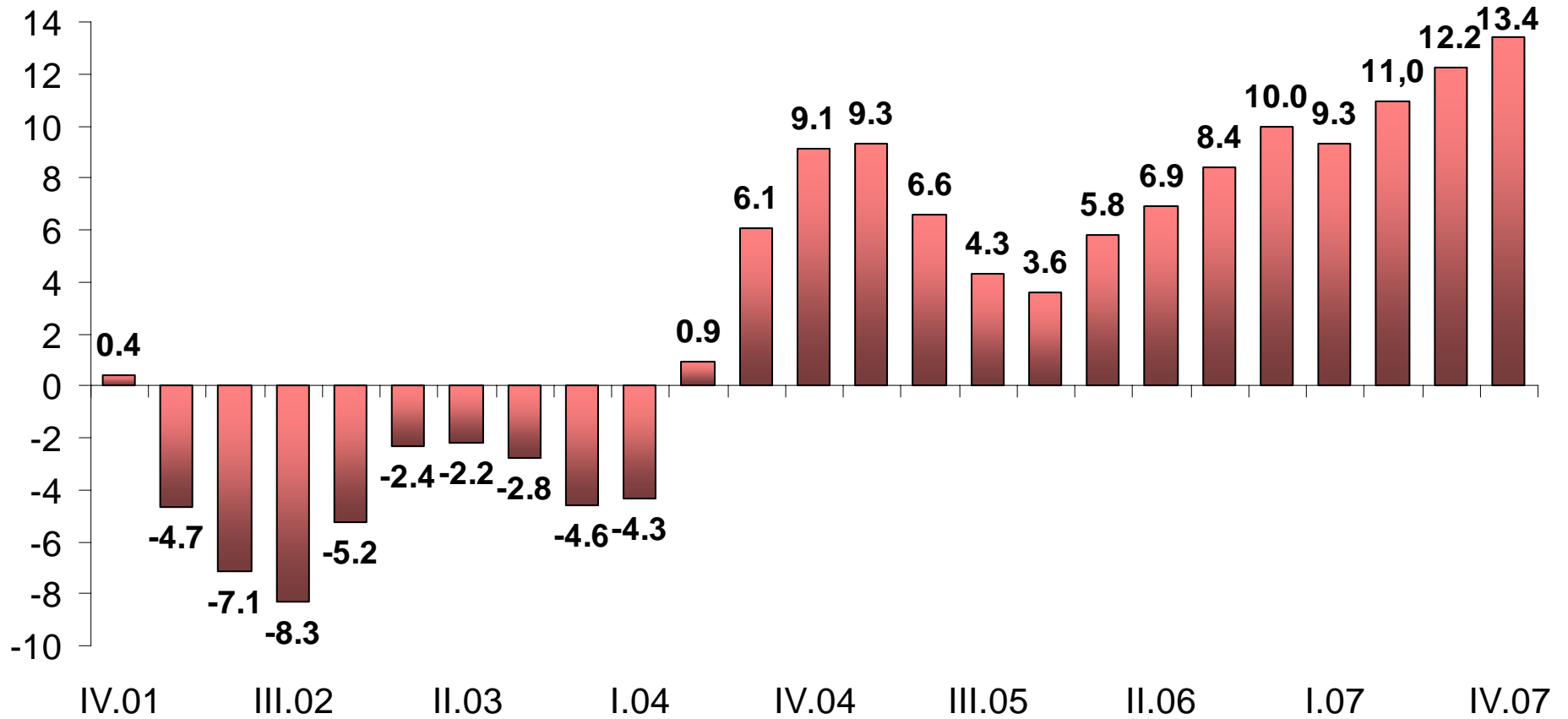
(% variation accumulated in the last 4 quarters)





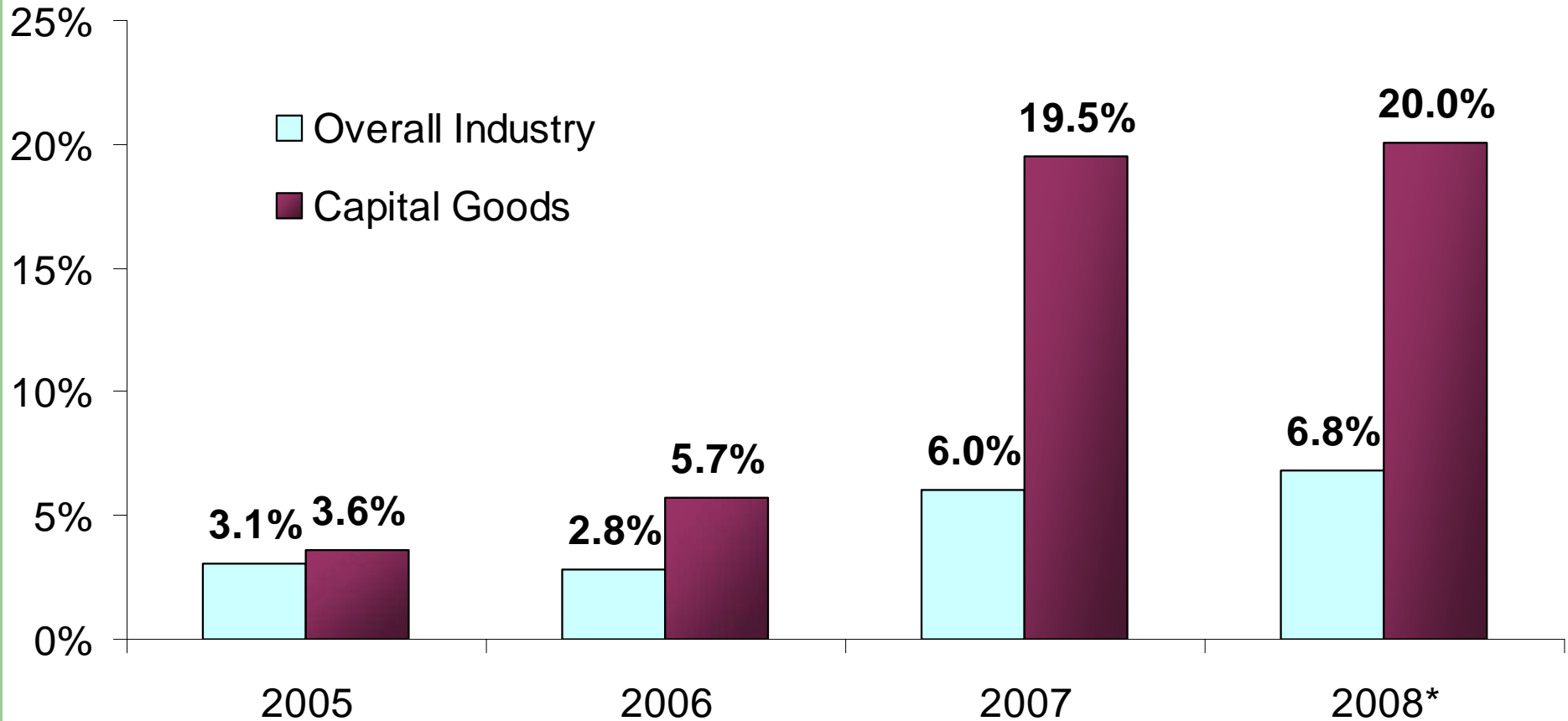
# INVESTMENT

(% variation accumulated in the last 4 quarters)





# INDUSTRIAL AND CAPITAL GOODS PRODUCTION (% growth rate)



\*/ 12-month cumulative up to February/08)

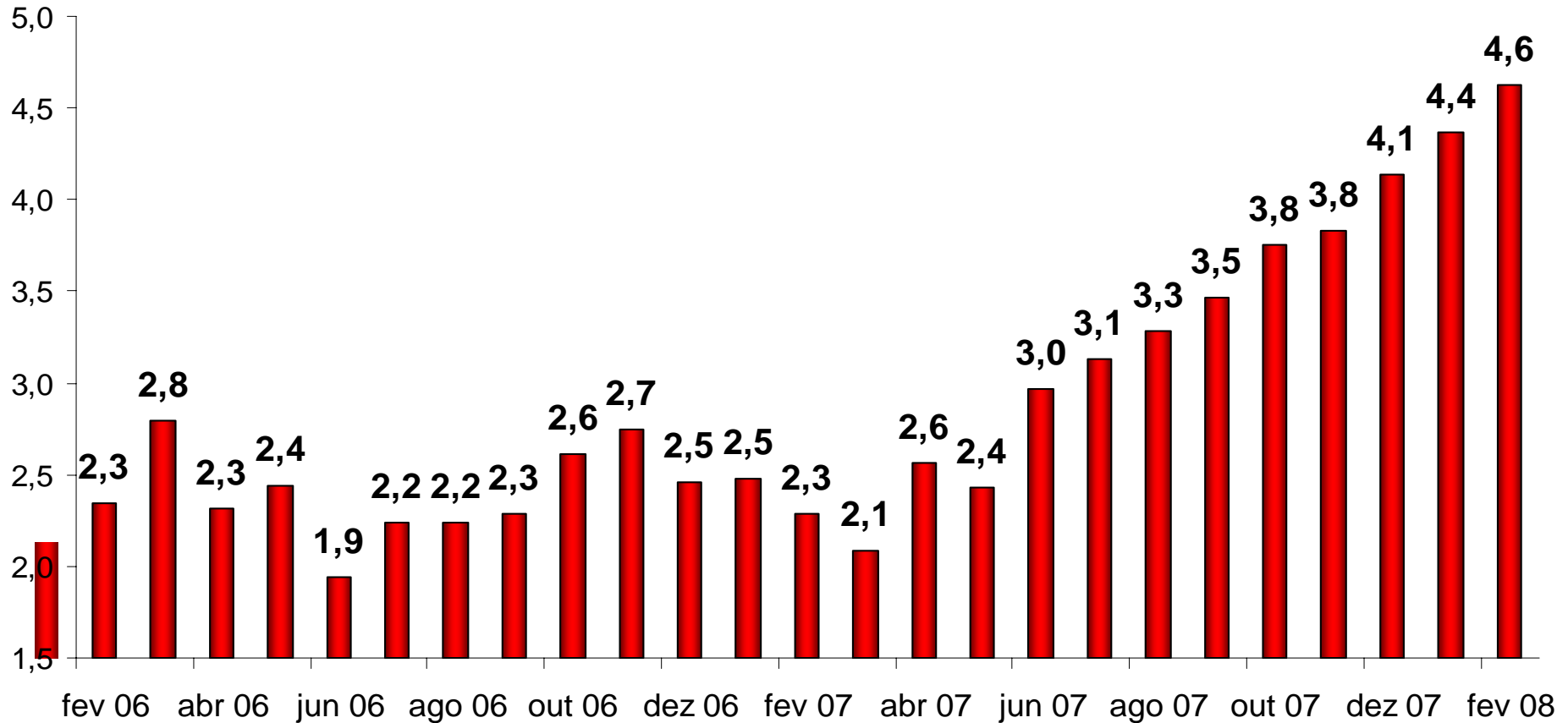
Source: IBGE.

Elaborated by: MF/SPE.



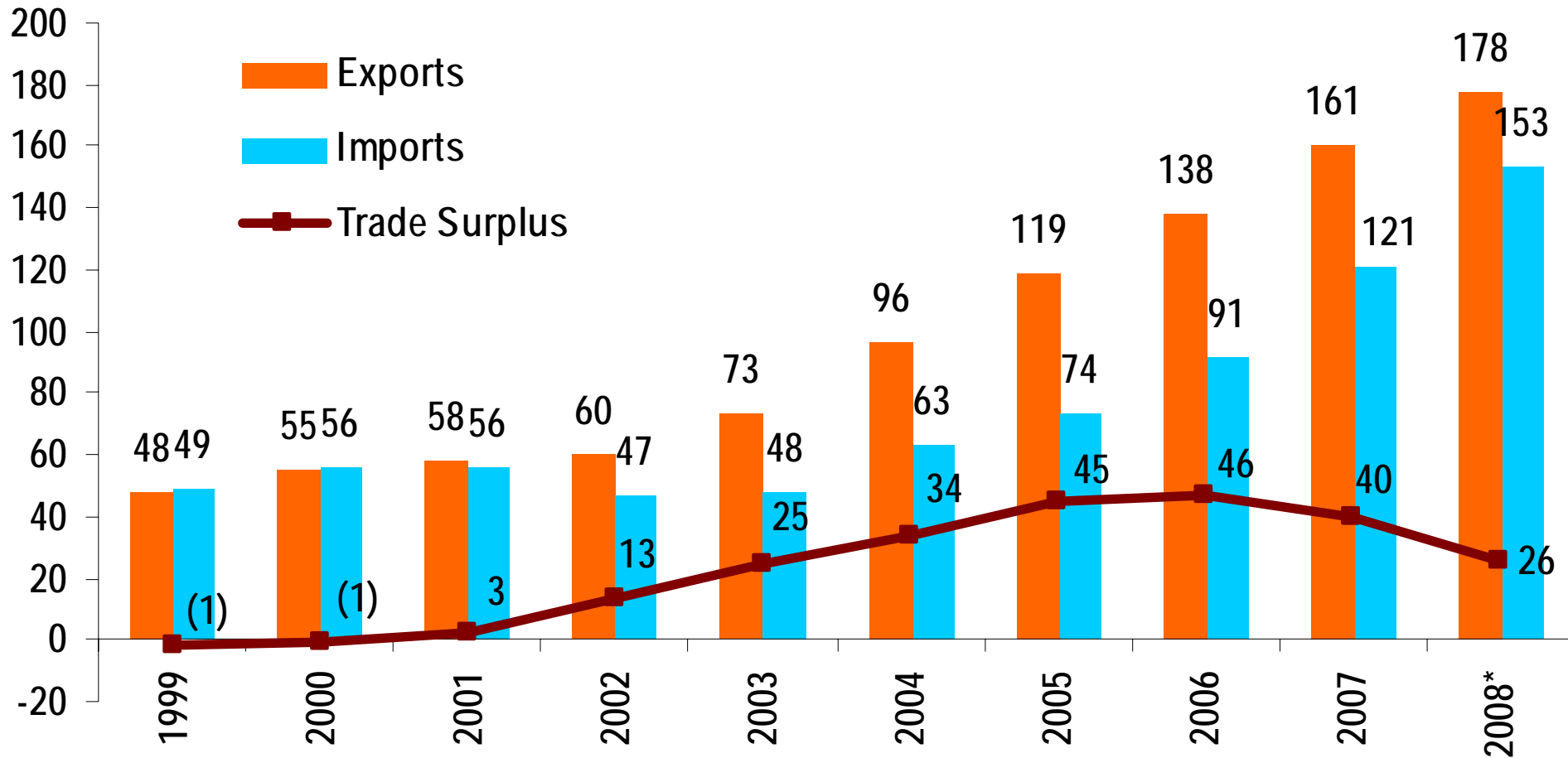
# PRODUCTIVITY

Industrial Production / Hours paid  
(12 month cumulative % variation)





# TRADE BALANCE (US\$ billions)



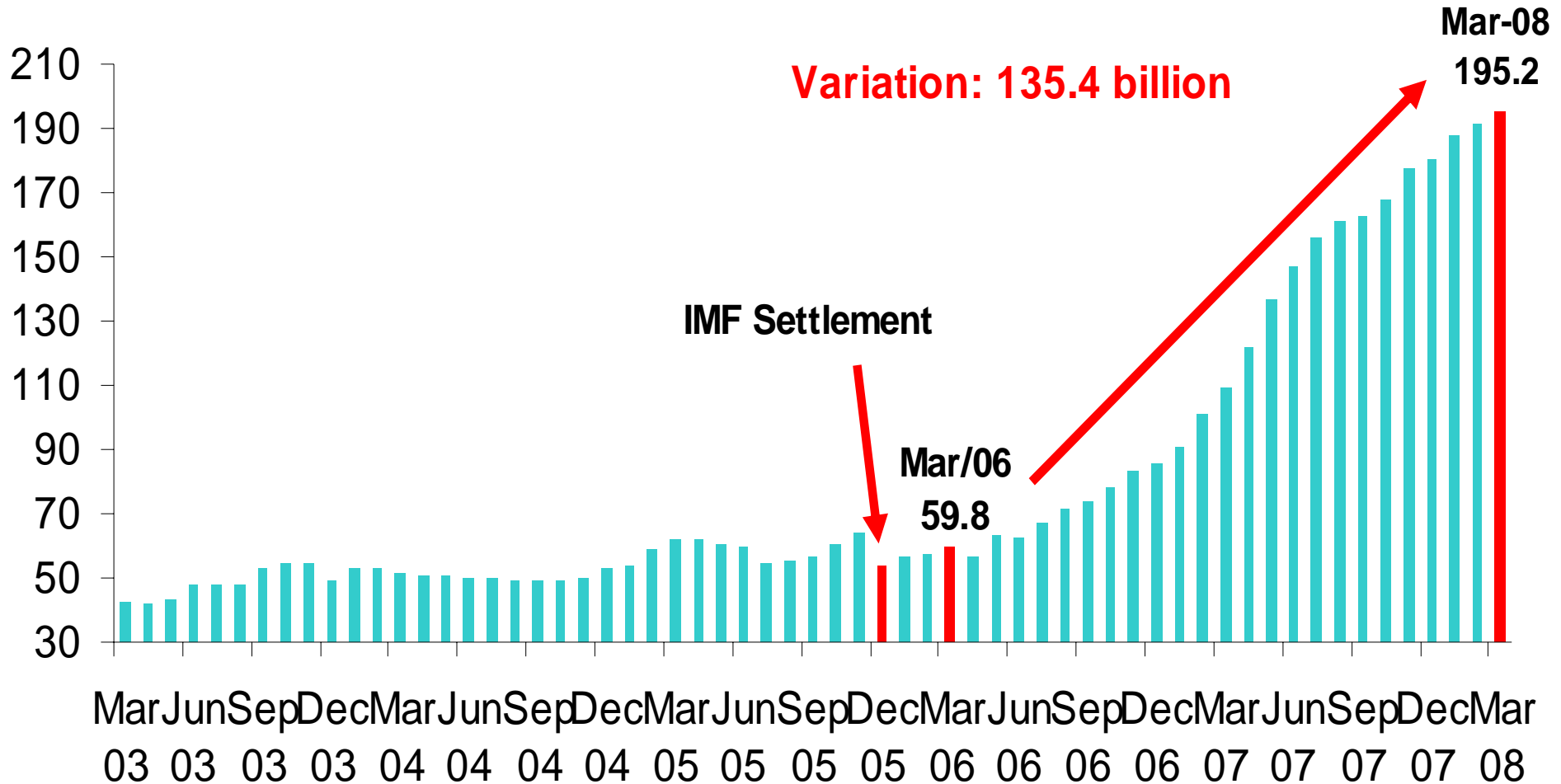
\*/ Market Expectations – Focus (04/04/2008)

Source: Ministry of Development, Industry and Foreign Trade.

Elaborated by: MF/SPE.



# INTERNATIONAL RESERVES (US\$ billion)

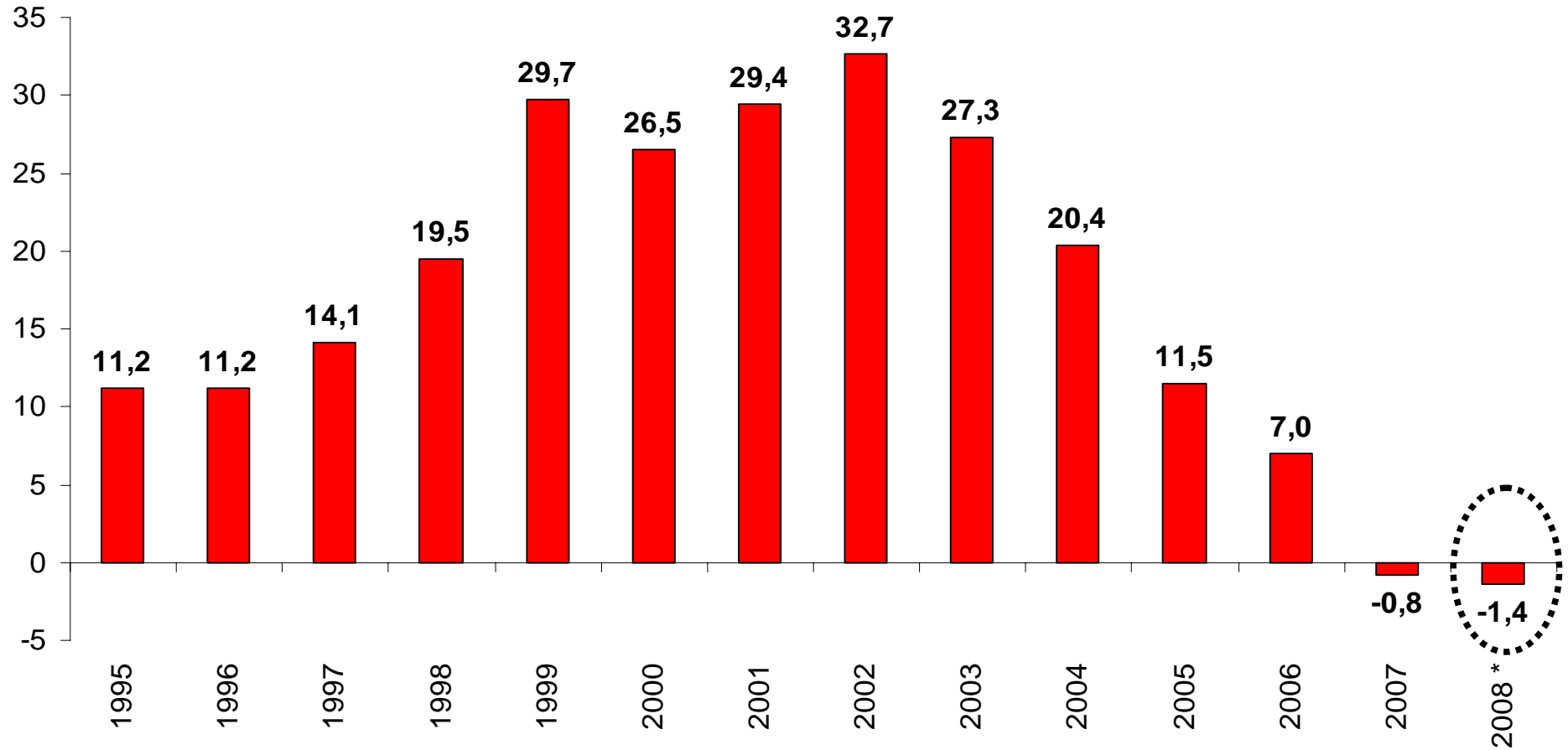


Source: BCB. Prepared by: MF/SPE.



# SOLVENCY INCREASE

(Net External Debt / GDP)



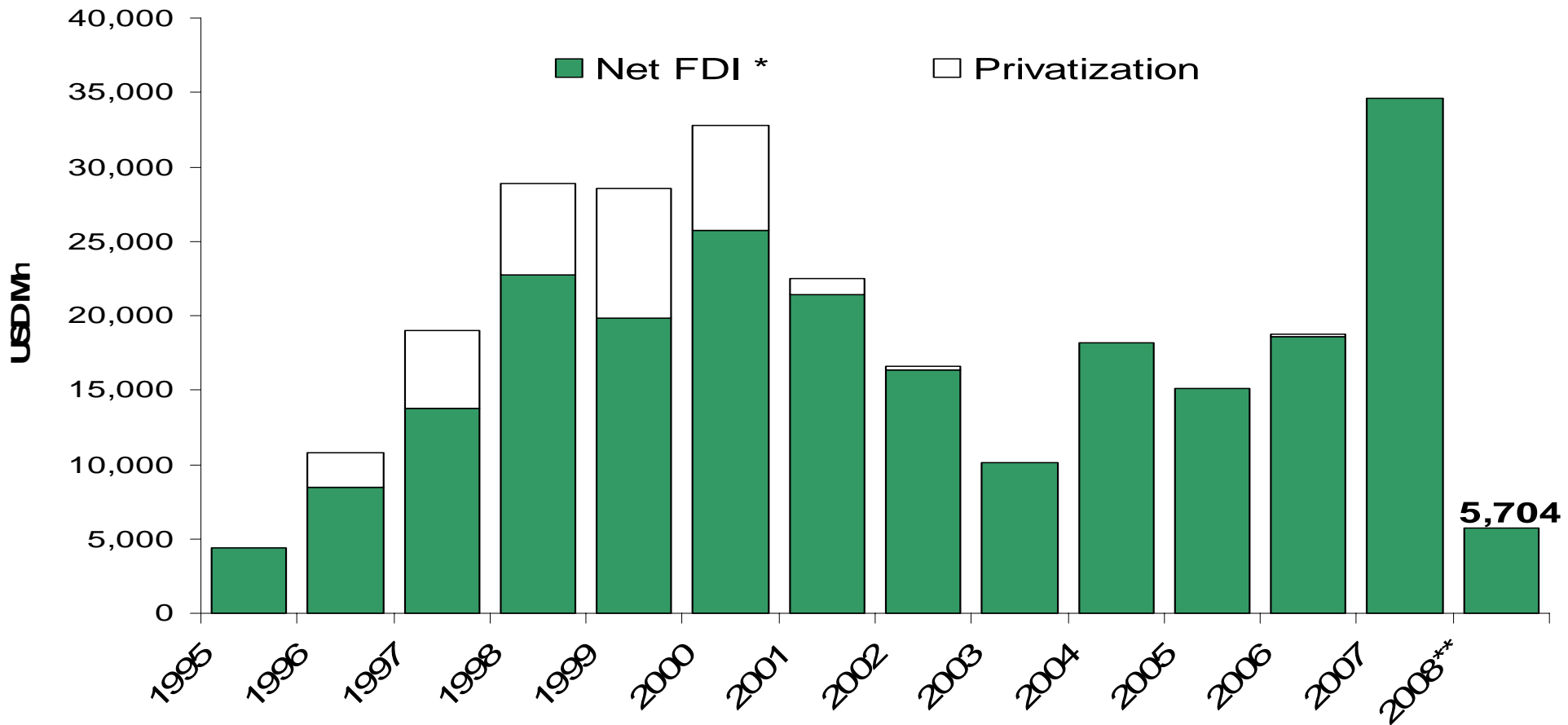
\*/ Estimated for Feb/08.

Source: BCB.

Elaborated by:MF/SPE



# Foreign Direct Investments



Source: Central Bank

\* No privatizations

\*\* Until Feb-08



# MASS CONSUMPTION AND NEW MIDDLE CLASS



## MASS MARKET

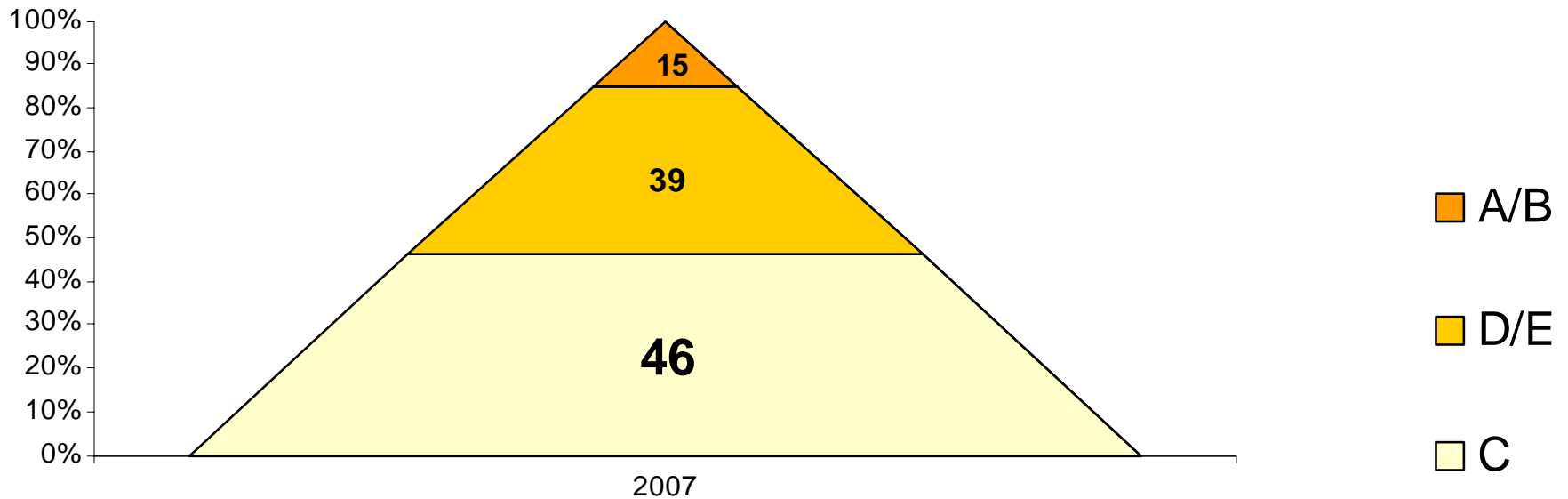
- Enhancement of the Population is Consumption Capacity
  - Expansion of employment and income
  - Minimum wage
  - Credit revolution
  - Expansion of social programs
  - Inflation under control
  
- Emerging New Middle Class



## NEW SOCIAL STRATIFICATION PYRAMID

(Social mobility of the Brazilian population)

Nowadays, Class C (middle class) represents the base of the social pyramid in Brazil, accounting for 86.2 million people. Between 2006 and 2007, this social segment increased its share from 36% to 46% mainly because of up award mobility from the lower-level classes (Classes D/E).



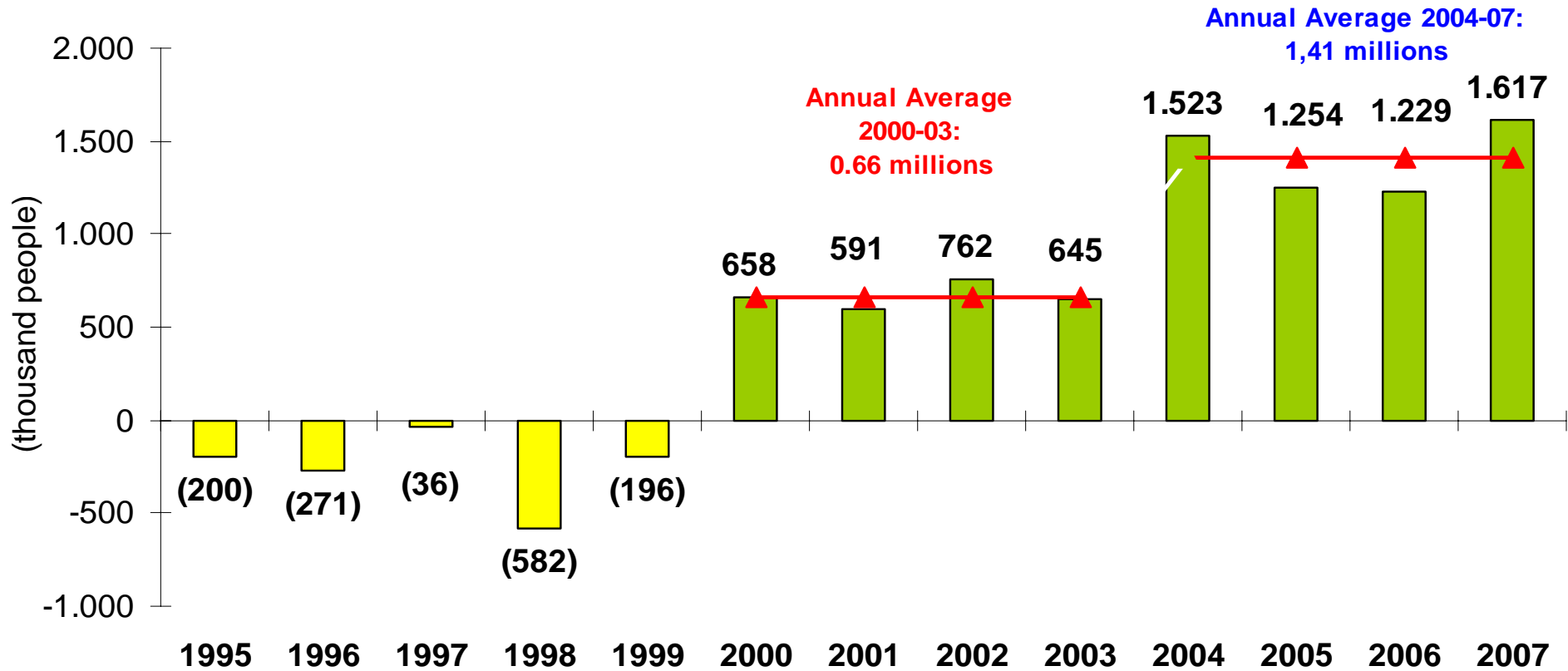
\*/ Social classification includes income, wealth and education; class A/B: R\$2,217; class C: R\$1,062; class D/E: R\$850.

Source: IPSOS Research (O Estado de São Paulo, page B16, 30/03/2008).



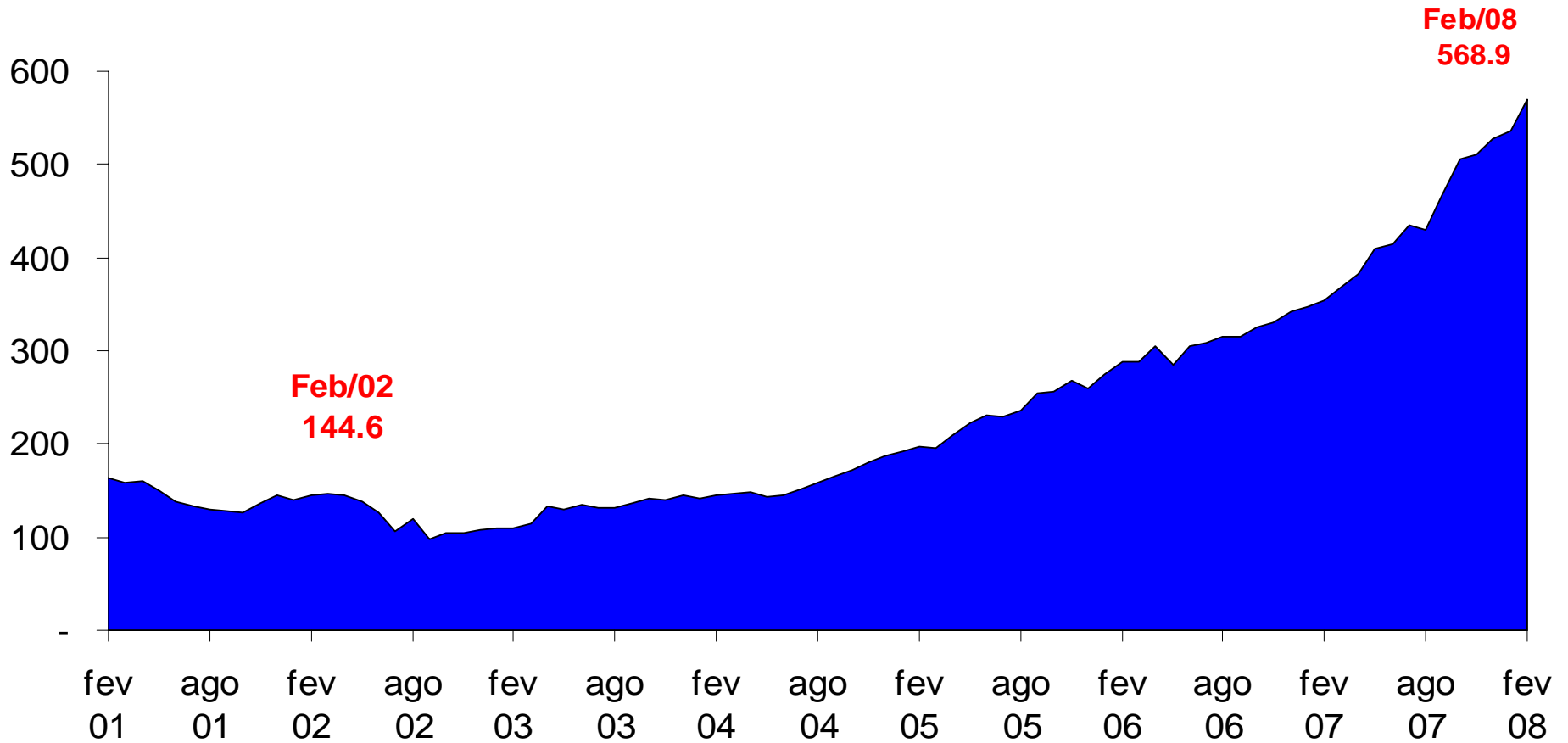
# EMPLOYMENT CREATION

5.6 million of new formal jobs were created between 2004 and 2007.





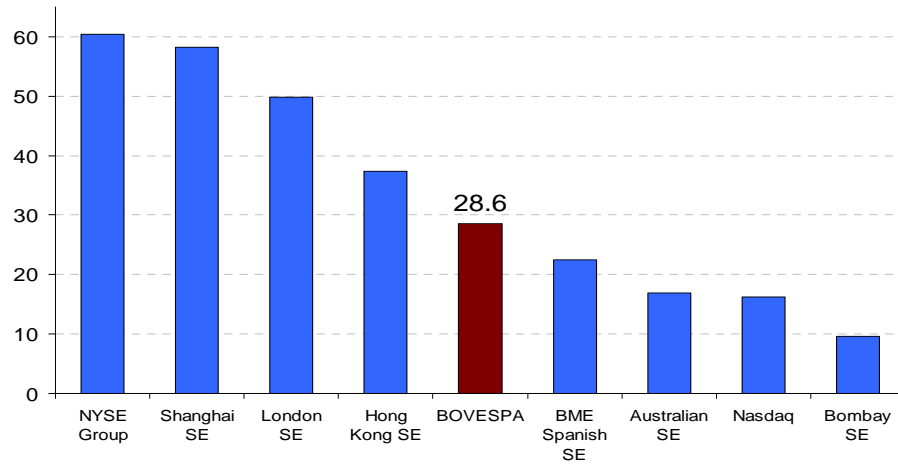
# VOLUME OF TOTAL BANK CREDIT (US\$ billions)





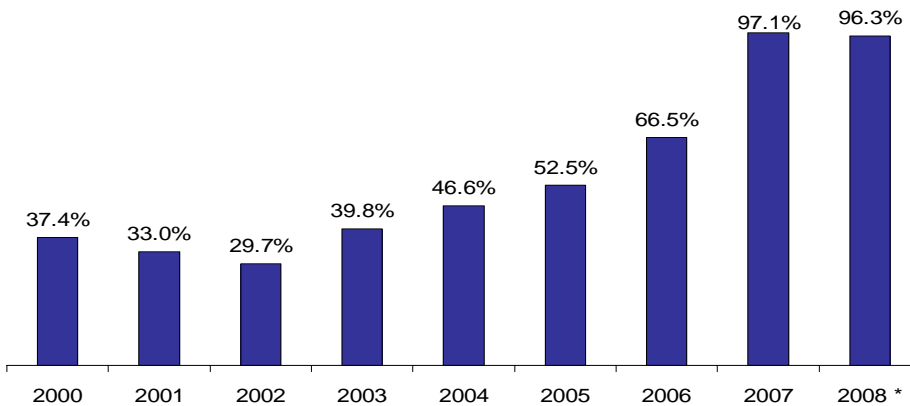
## Capital Market booming

### IPO's in 2007 (US\$ Billion)



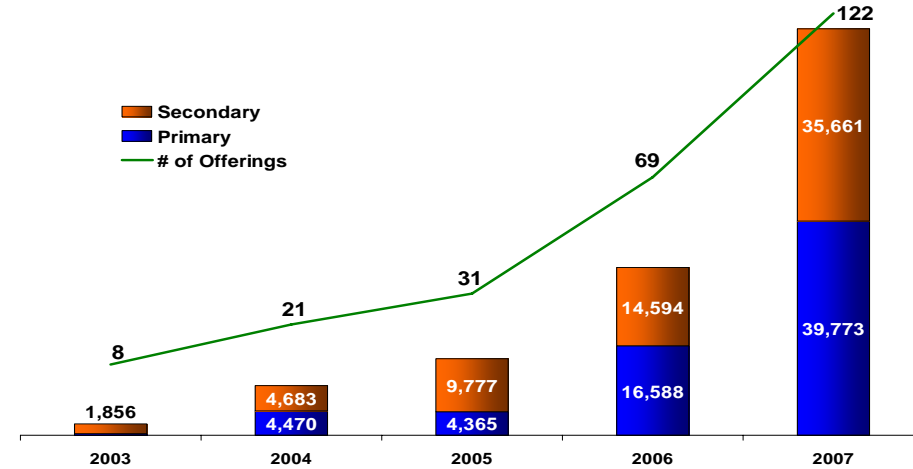
Source: WFE

### Stock Market Value (% GDP) - Bovespa



Source: Bovespa, IBGE and Central Bank \* January

### Stock - Public Offering (R\$ Mn)

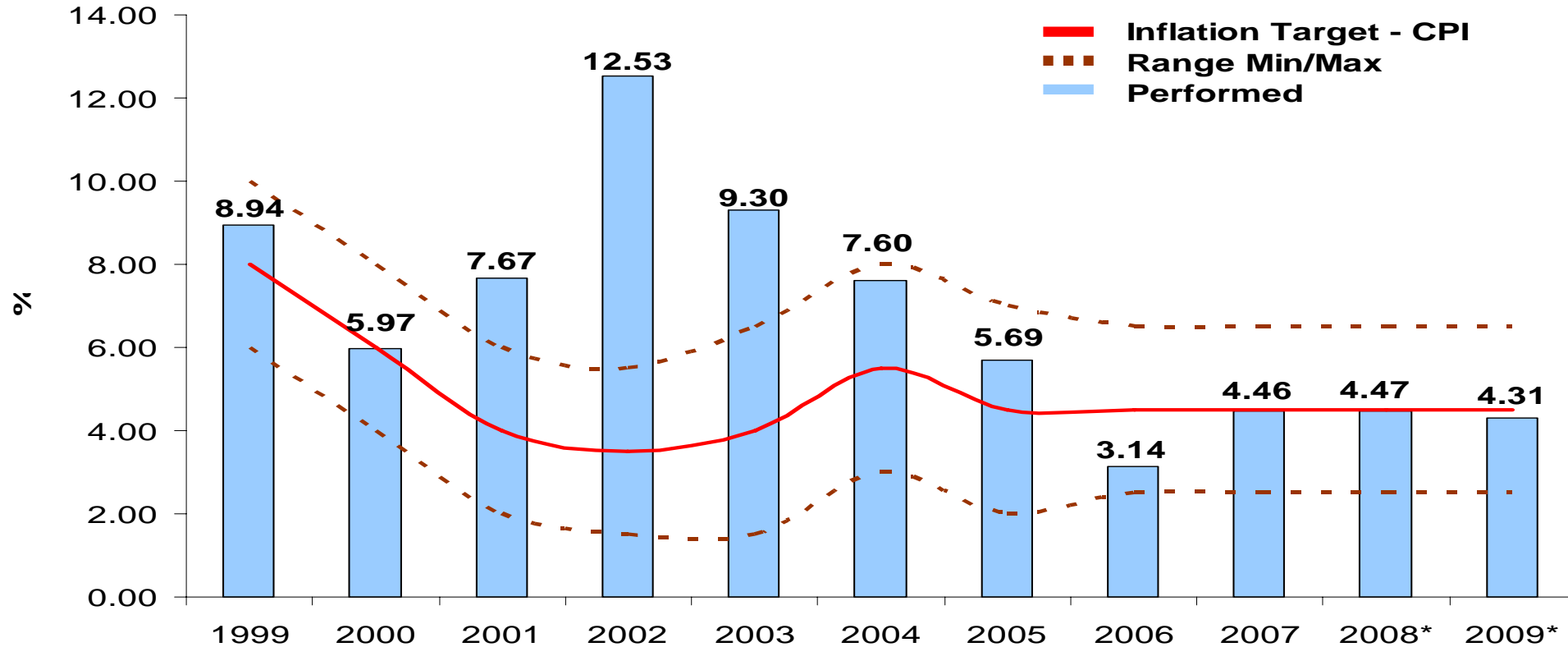


Source: CVM

- BOVESPA Market Capitalization achieved R\$ 2.4 trillion in February 2008.
- According to MSCI index, Brazil is now the largest Emerging Market in the world, representing 14.95% of the index.
- Bovespa and BM&F announced a merger agreement that will create the 3<sup>rd</sup> biggest exchange in the world in market value.



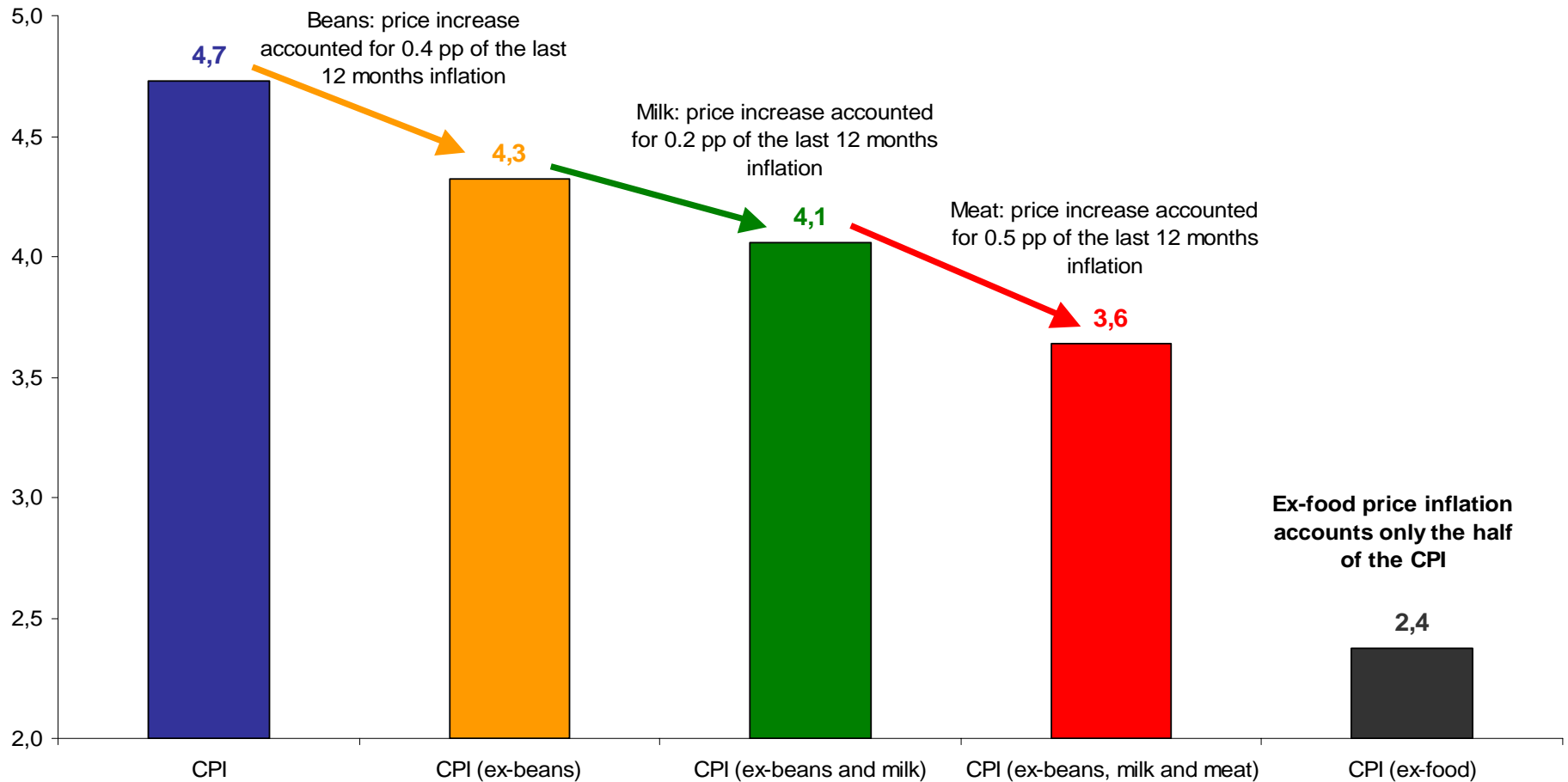
## Annual Inflation Effective, Expectation and Target



- Inflation below the upper limit since 2004 and below the targets since 2006.
- Inflation is near the target and below the upper limit for 2008 and 2009.
- Medium and Long Term Real interest rate below 7% during 2007, against 9% in 2005 and 8% in 2006.



## Impacts of Food Price Inflation\*



\*/ Accumulated in the last 12 months until March/08.

Source: IBGE.

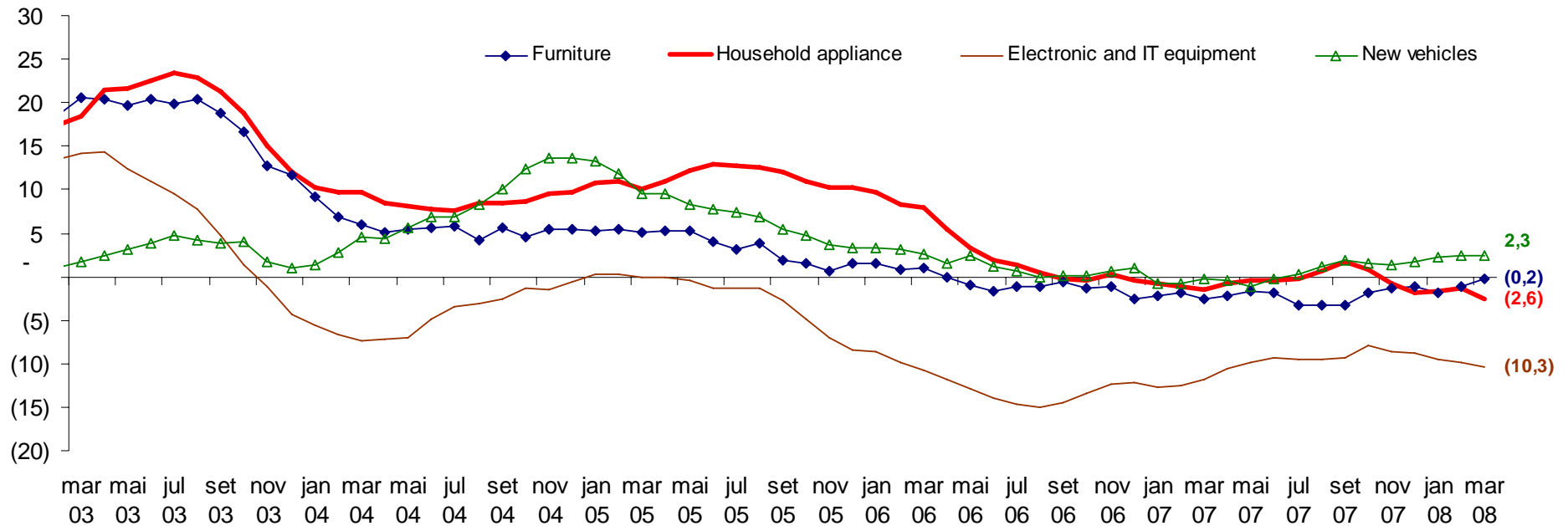
Elaborated by: MF/SPE.



## Industrial Products Inflation

Besides the rise in demand, driven by the expansion of banking credit, durable goods inflation is under control due to bigger trade openness regarding imports. There is deflation in the majority of items and, in the case of automobiles, the inflation is much below the 4.5% midpoint target. Nevertheless, the biggest deterioration risks are related to the increase in price of industrial inputs.

### Inflation Accumulated in the last 12 months

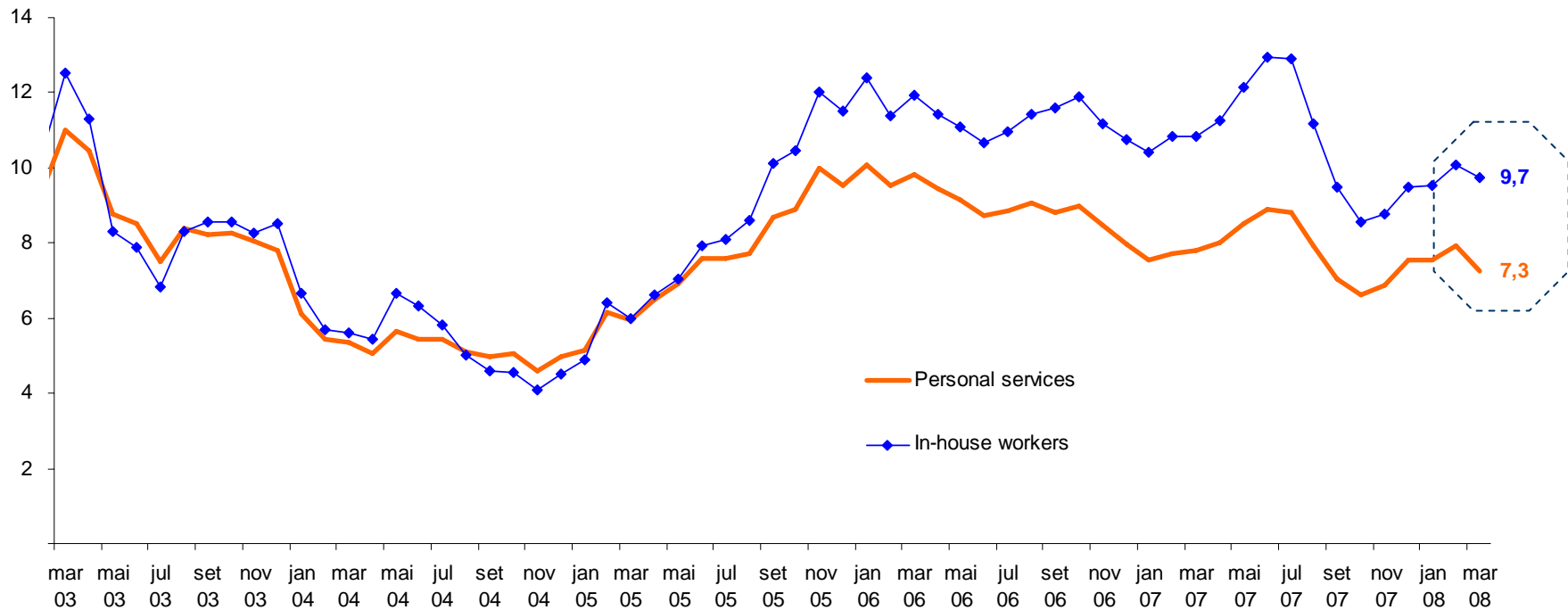




## Services Inflation

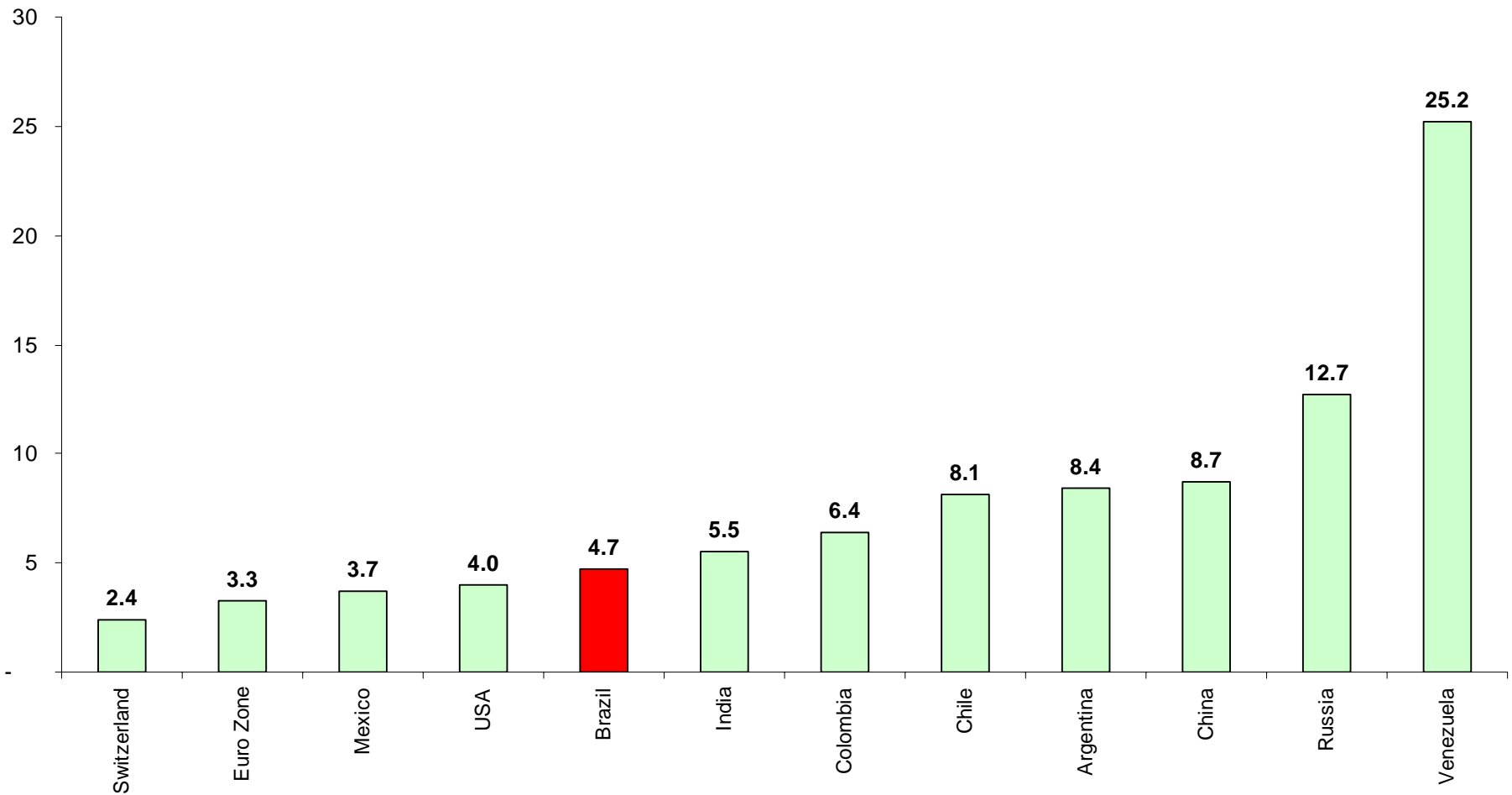
Price of Service is inflation decelerated in the 3rdQ/07. However, it has had an upward trend since then. Aside from this negative scenario, the current figures are below the ones observed at mid2007 and they reflect a combination of conjunctural (creation of new jobs and increase in wages) as well as structural (government policies, preferences and productivity) factors.

Inflation Accumulated in the last 12 months





## INFLATION VARIATION OF THE CONSUMER PRICE INDEX\*



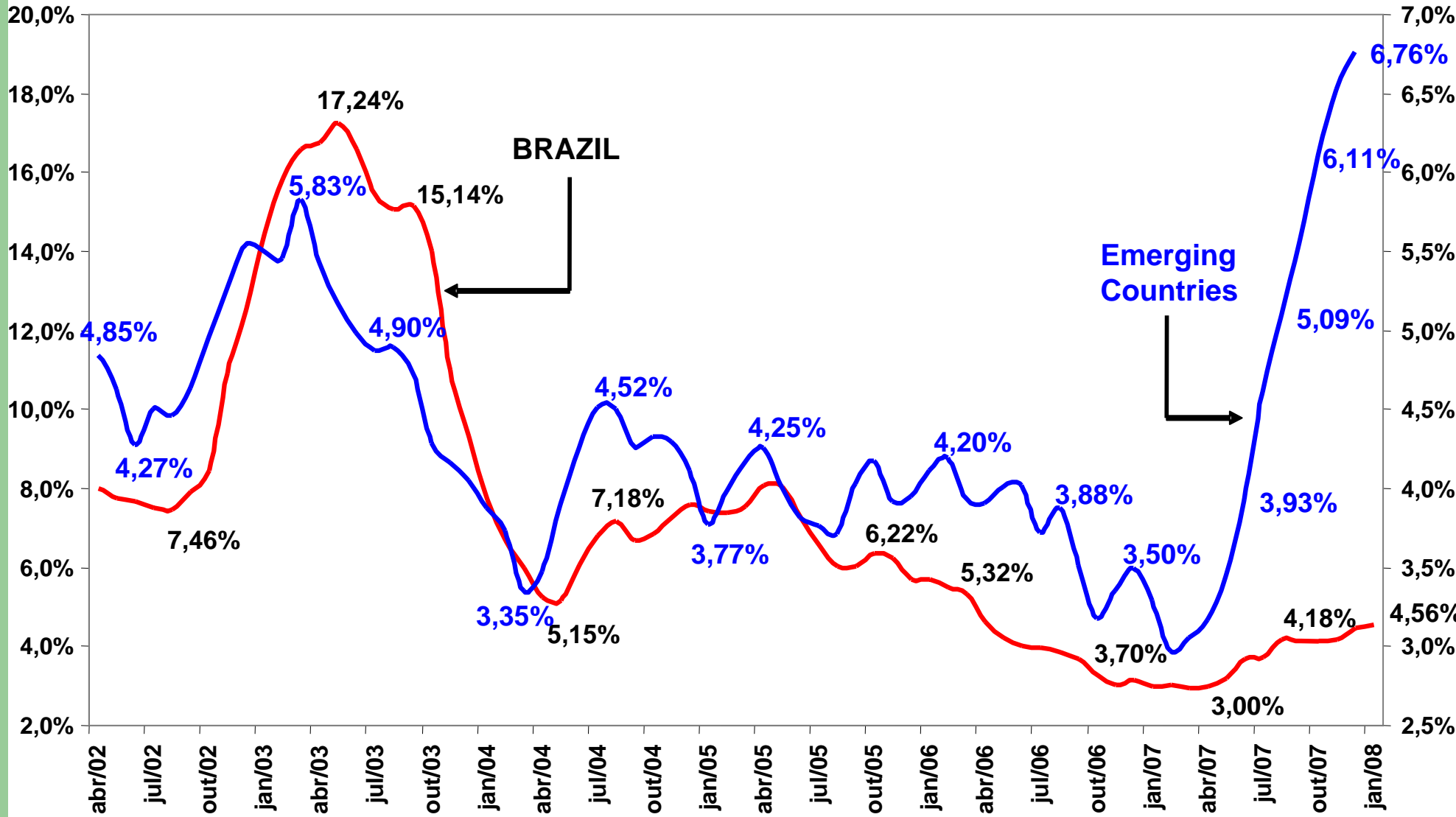
\*/ Accumulated in the last 12 months up to Feb/08 for all countries, except for India, where such timeframe ends in Jan/08.

Source: The Economist (March 29th 2008).

Elaborated by: MF / SPE.



## INFLATION IN BRAZIL AND EMERGING COUNTRIES – ACCUMULATED 12 MONTHS 2001 A 2008





## INFLATION TARGET MONITOR AND NEXT RATE MOVE

	Inflation target	Latest Month	12M MS FCast	Next Rate Decision	Current Rate	Market Expects (bp)	MS Expects (bp)
US	1.8% core PCE (u)	2.0%	1.9%	30-Apr	2.25	-35	-50
Euro Area	< 2% HICP (u)	3.5%	2.1%	10 Apr	4.00	0.1	0
Japan	0-2% CPI (u)	1.0%	0.9%	30 Apr	0.50	-3	0
UK	2% CPI	2.5%	2.4%	10 Apr	5.25	-23	-25
Canada	1-3% on CPI	1.8%	2.0%	22 Apr	3.50	-40	-50
Switzerland	<2% CPI (u)	2.4%	2.1%	19 Jun	2.75	-8	0
Sweden	2.0% CPIX	2.0%	2.1%	23 Apr	4.25	-6	0
Norway	2.5% CPI-ATE	2.2%	2.1%	23 Apr	5.25	19	0
Australia	2-3% over the cycle	3.0%	3.8%	06 May	7.25	7	0
Russia	< 8.5% CPI end '08 (u)	13.3%	12.2%	-	6.25	-	-
Poland	2.5% (+/- 1%) CPI	4.2%	4.1%	30 Apr	5.75	28	25
Czech Rep.	3.0% (+/-1%) CPI	7.1%	3.1%	7 May	3.75	3	25
Slovakia	2% end-2008 CPI	3.8%	3.0%	29 Apr	4.25	-1	0
Hungary	3.0% (+/-1%) CPI	6.9%	3.7%	28 Apr	8.00	18	25
Romania	3.8 (+/-1%) CPI	8.0%	6.2%	06 May	9.50	0	0
Ukraine	< 9.6% CPI end '08 (u)	26.2%	19.5%	-	10.00	-	-
Turkey	4% CPI	9.2%	5.5%	17 Apr	15.25	0	0
Israel	1 - 3% CPI	3.6%	2.0%	28 Apr	3.25	0	0
South Africa	3-6 % CPIX	9.4%	7.4%	10 Apr	11.00	10	50
Nigeria	-	8.0%	5.4%	5 June	10.00	-	0

(u) = unofficial Note: Inflation numbers in red indicate values above target; MS expectations in red (green) indicate our rate forecasts are above (below) market expectations Source: National Central Banks, Morgan Stanley Research

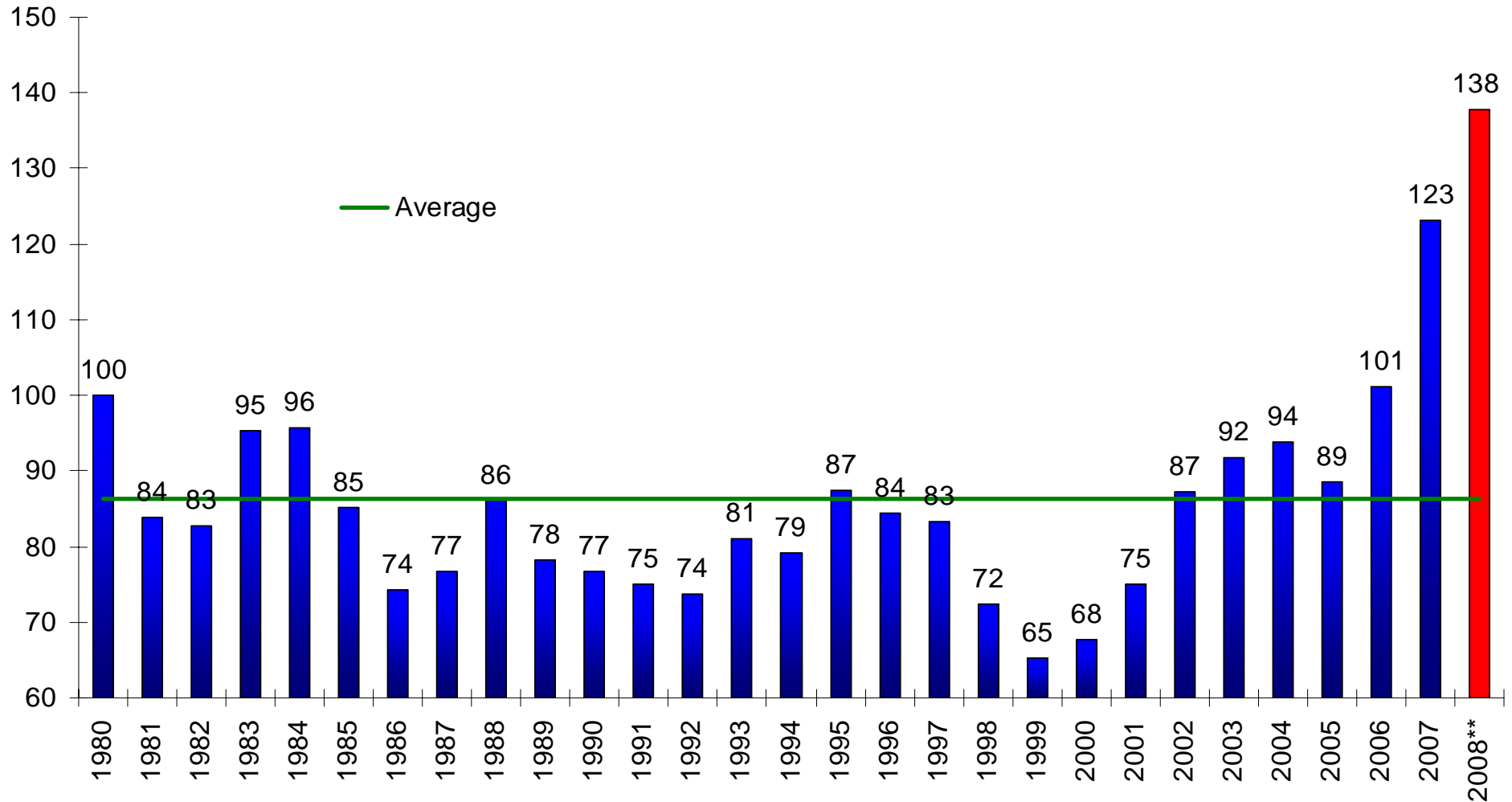


## INFLATION TARGET MONITOR AND NEXT RATE MOVE

	Inflation target	Latest Month	12M MS FCast	Next Rate Decision	Current Rate	Market Expects (bp)	MS Expects (bp)
China	4.8%	8.7%	6.5%	-	7.47	0	0
India	5.0% WPI	7.0%	4.7%	29 Apr	7.75	-	0
Hong Kong	-	6.3%	4.5%	-	4.50	-50	-75
Korea	2.5% - 3% CPI	3.9%	3.0%	10 Apr	5.00	0	0
Taiwan	-	4.0%	3.0%	27 Jun	3.50	0	0
Singapore	1.5% (Long-term CPI) (u)	6.5%	4.8%	10 Apr	1.38	-	-
Indonesia	6.0%-6.5% CPI	8.2%	7.1%	08 May	8.00	0	0
Philippines	3.0%-5.0% CPI	6.4%	5.3%	13 Apr	5.00	0	0
Malaysia	-	2.7%	2.6%	29 Apr	3.50	0	0
Thailand	2.8%-4.0% CPI	5.3%	4.0%	21 May	3.25	0	0
Brazil	4.5% +/- 2.0%	4.6%	4.3%	16 Apr	11.25	25	0
Mexico	3% (+/-1%, CPI)	3.7%	3.8%	18 Apr	7.50	0	0
Argentina	15.5-24.2% M2 Growth	8.4%	10.5%	NA	8.63	-	-
Chile	3% (+/-1%, CPI)	8.5%	4.1%	10 Apr	6.25	0	0
Peru	1%-3% CPI	5.5%	2.9%	10 Apr	5.25	0	0
Colombia	3.5%-4.5% CPI	5.9%	5.8%	25 Apr	9.75	0	0



# CRB Foodstuffs Sub-index \* (1980=100)



\*/ End of period.

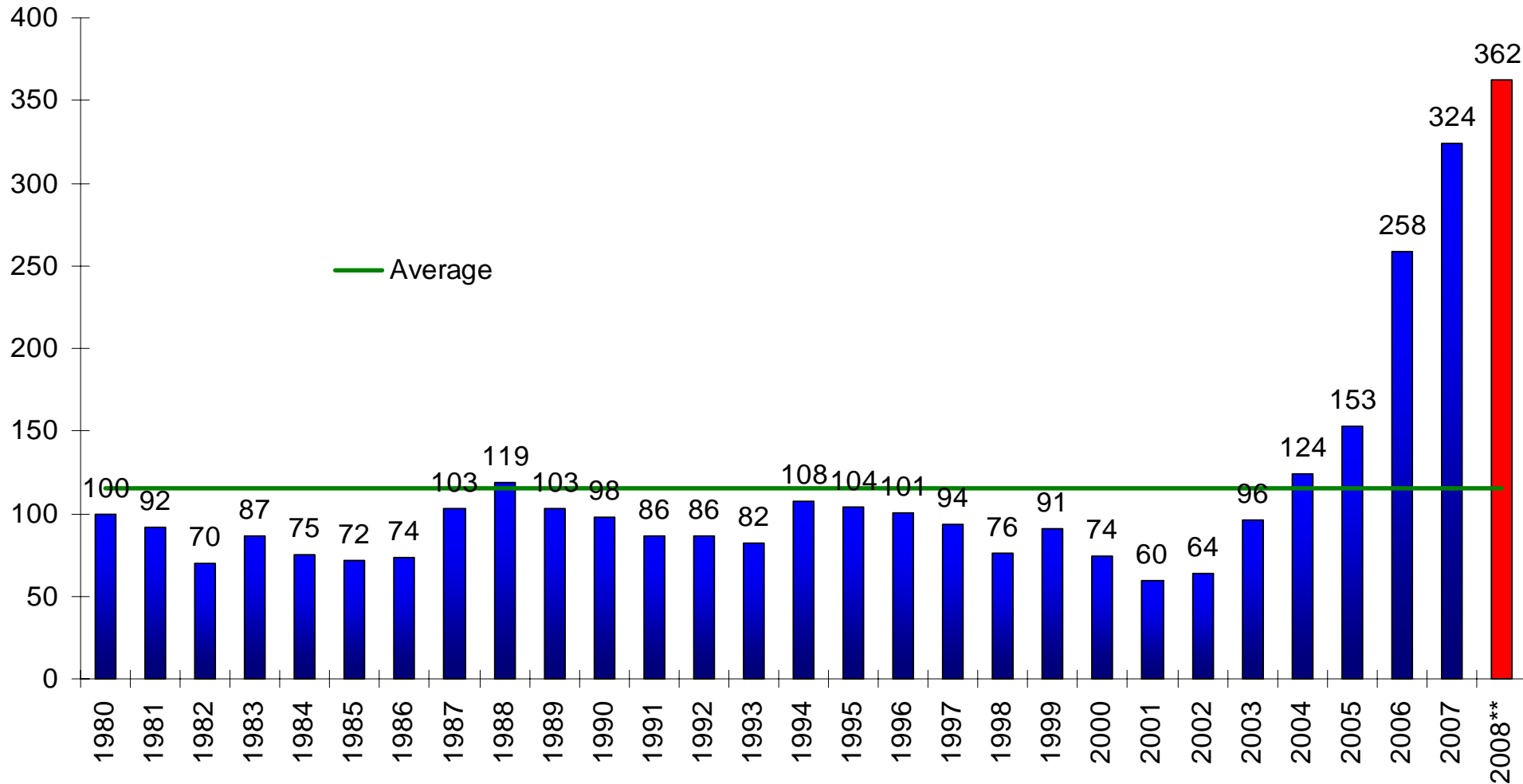
\*\*/ March, 2008

Source: CRB

Elaborated by: MF/SPE



# CRB Metals Sub-index\* (1980=100)



\*/ End of period.

\*\*/ March, 2008

Source: CRB

Elaborated by: MF/SPE

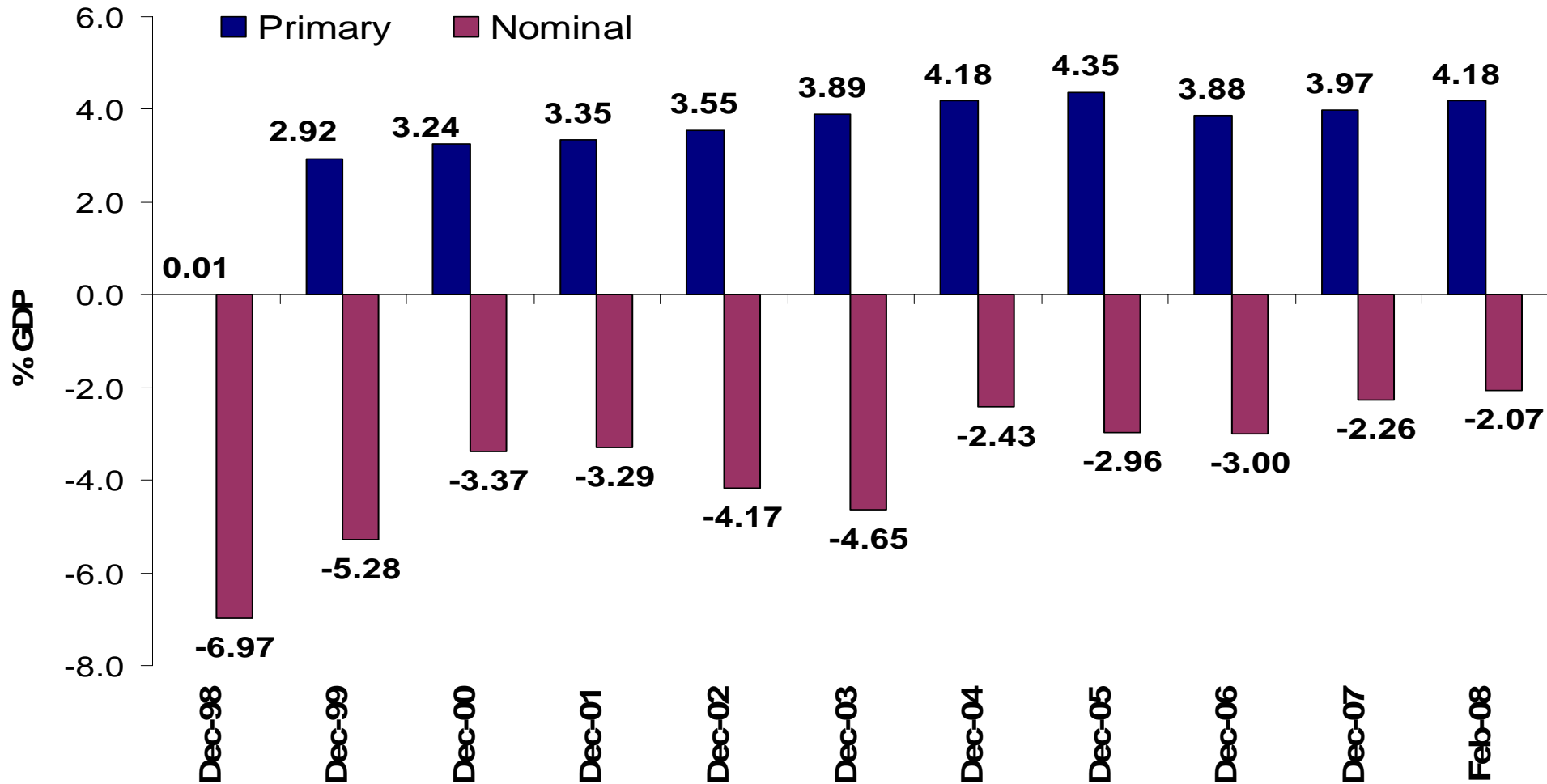


# FISCAL COMMITMENT



## Fiscal Commitment

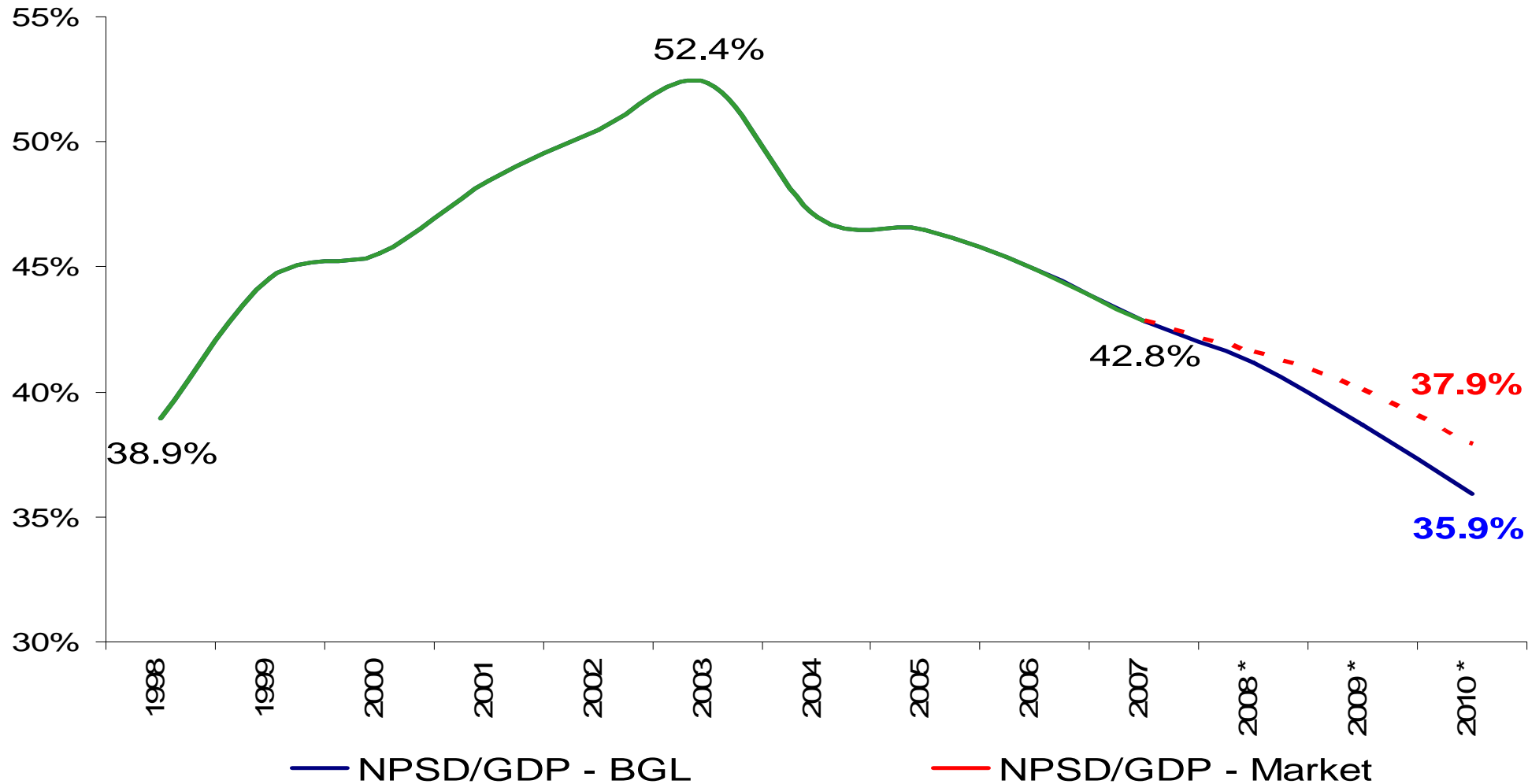
### Public Sector Balance (in 12 months)





## Fiscal Commitment

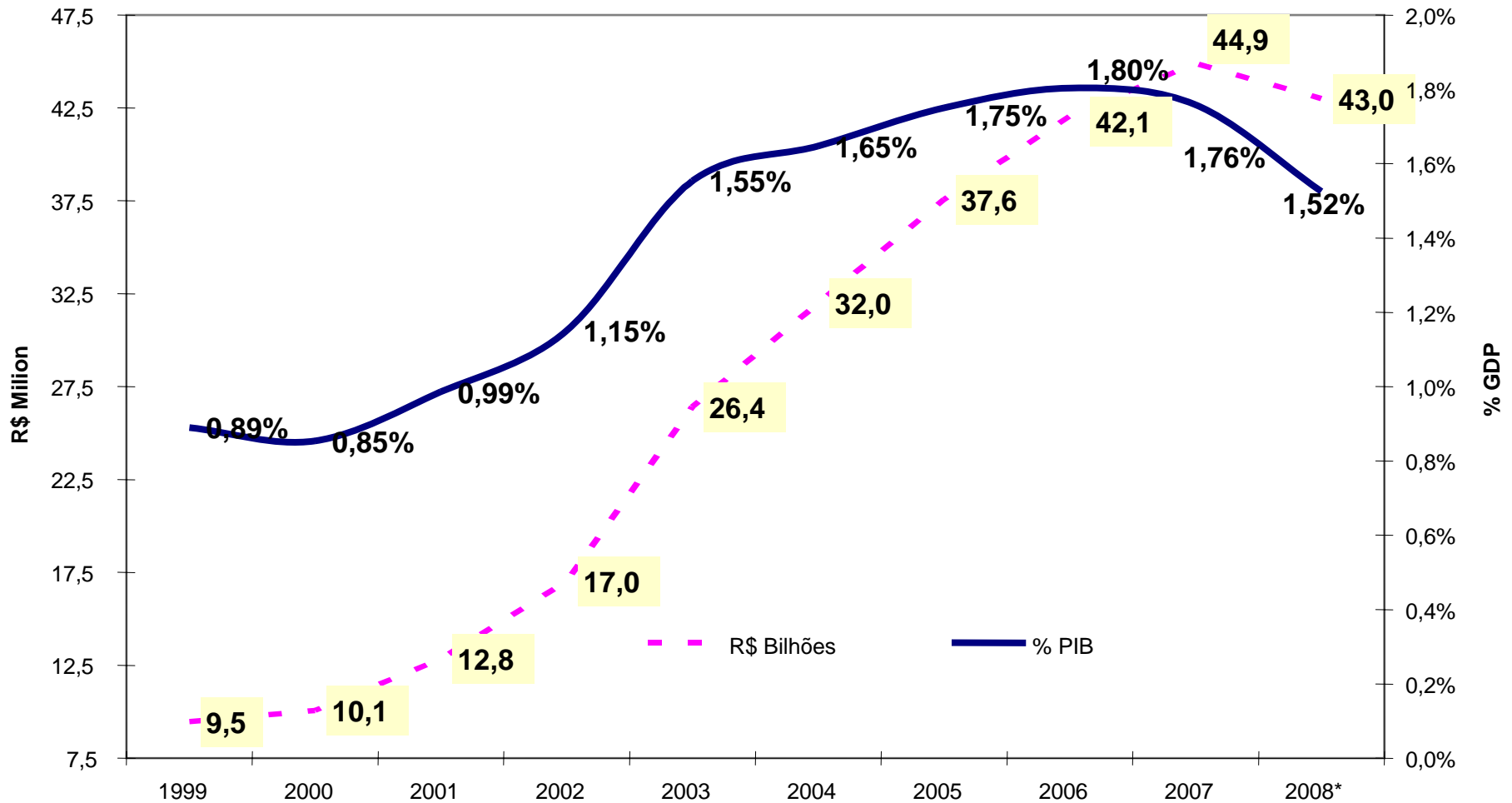
# Net Public Sector Debt / GDP





# Social Security Deficit – 2008 Budgetary Law

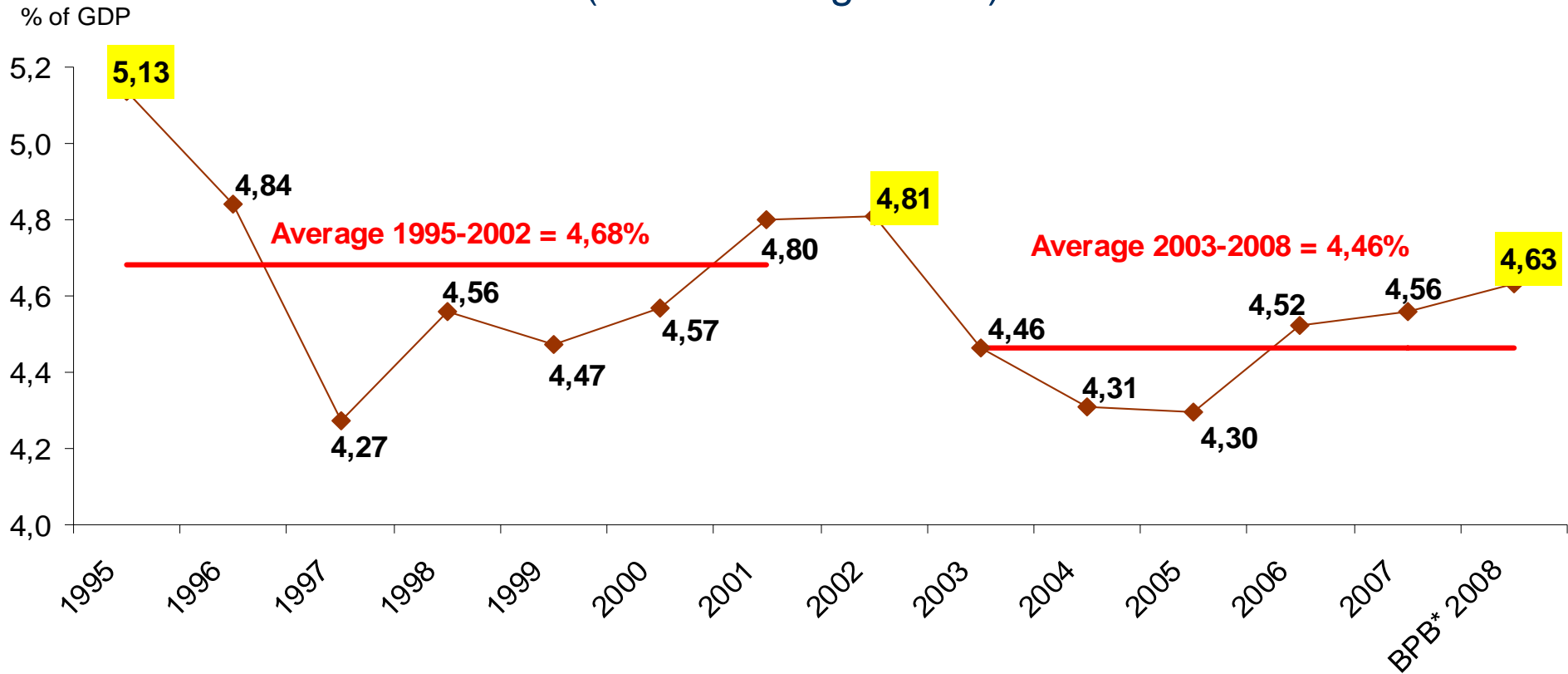
Better perspectives for public sector social security, reflecting the 1998 and 2003 reforms, which extended the retirement age and taxed retirees.





# EVOLUTION OF TOTAL GOVERNMENT PAYROLL

(Not including CPSS)



\*/ Budget Proposal Bill

Source: MPOG/SOF.

Prepared by: MF/SPE.

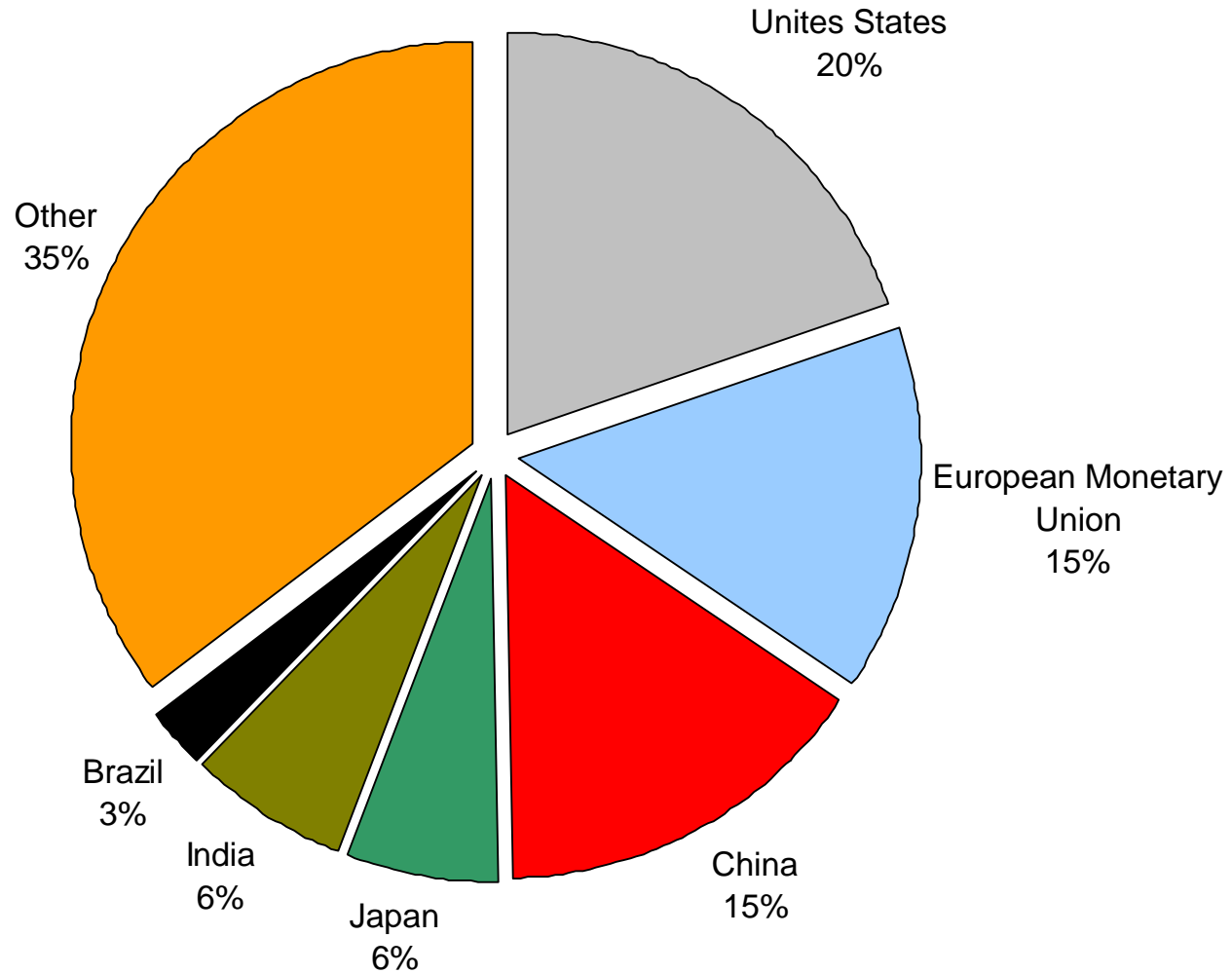


# WORLD ECONOMY: NEW GROWTH DYNAMICS



# COMPOSITION OF WORLD GDP (PPP)

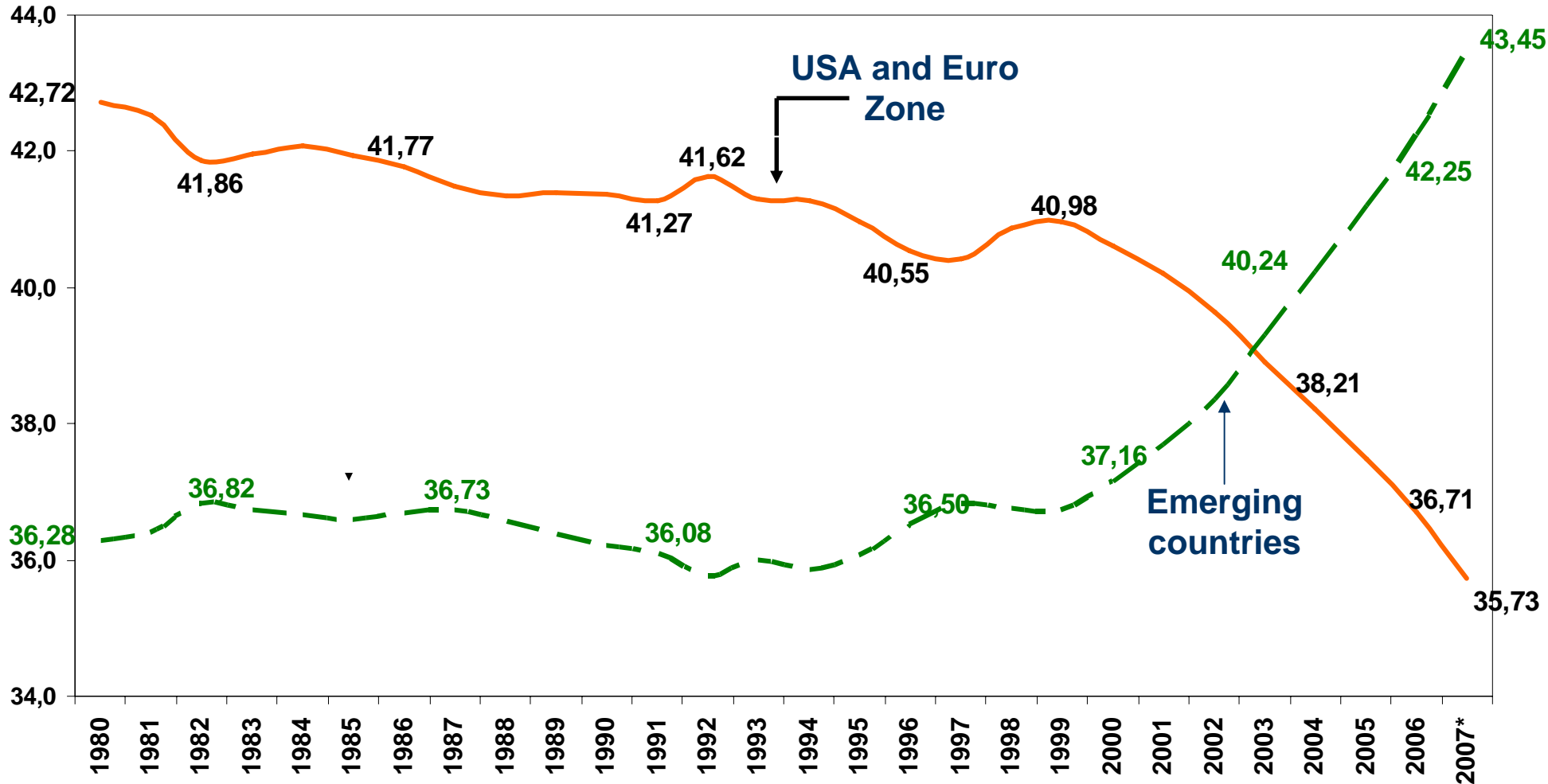
World GDP in 2006 reached US\$ 66.8 trillions



Source: World Development Indicators Database



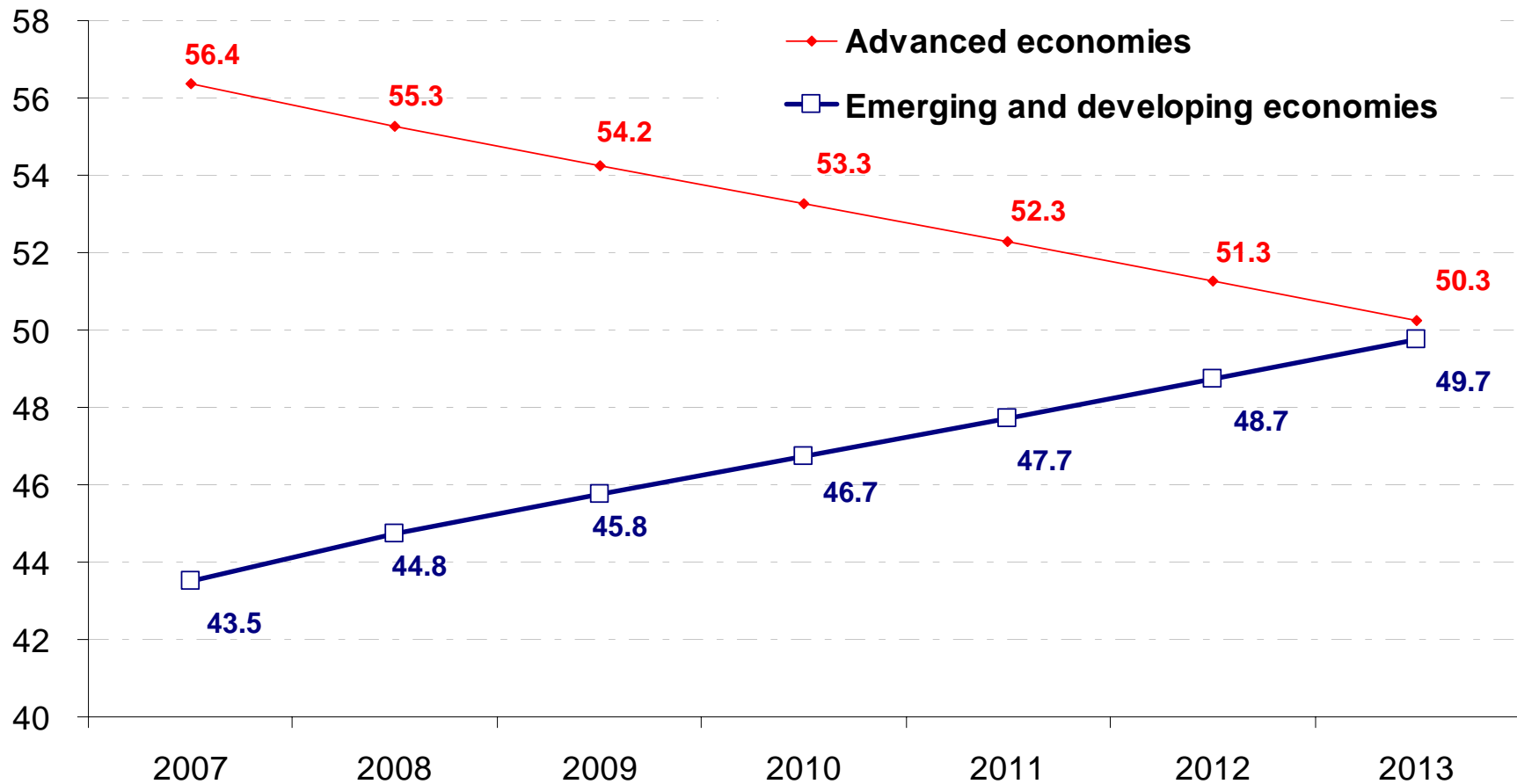
# USA AND EUROZONE vs. EMERGING COUNTRIES PARTICIPATION IN GLOBAL GDP (%) 1980 - 2007





# GROSS DOMESTIC PRODUCT BASED ON PURCHASING-POWER-PARITY (PPP)

(share of world total)





# GROWTH ACCELERATION PROGRAM (PAC)



## GROWTH ACCELERATION PROGRAM (PAC)

**PAC's main objective is to increase Brazil's volume of investment and to expand potential growth:**

- Increase Investment in Infrastructure
- Enhance the Investment Climate
- Improve the Tax System
- Stimulate the Credit Market
- Improve Long-Term Fiscal Policy



## GROWTH ACCELERATION PROGRAM (PAC)

- **Infrastructure investment program (2007-2010).**

	<b>R\$ bn</b>	<b>% of GDP</b>
<b>Total</b>	<b>503.9</b>	<b>4.36%</b>
<b>Federal Budget</b>	<b>67.8</b>	<b>0.59%</b>
<b>Private Sector (incl. state-owned companies)</b>	<b>436.1</b>	<b>3.77%</b>



## GROWTH ACCELERATION PROGRAM INVESTMENTS IN ENERGY

Program	Investment (R\$ bi)	
	Up to 2010	After 2010
Electric Power Generation	65.9	20.7
Electric Power Transmission	12.5	3.4
Oil and Gas	179.0	138.1
Renewable Fuel	17.4	27.0
<b>TOTAL</b>	<b>274.8</b>	<b>189.2</b>



## PAC – Growth Acceleration Program

### Aims for the future

- Energy (Hydroelectric, Thermonuclear and Thermoelectric power plants): 39,081 MW up to 2015
- This corresponds to an increase of roughly 40% of current electric energy installed capacity.

#### Main Projects in Course

TYPE	PROJECT	Investment (R\$ bn)	POWER (MW)
Hydroelectric power plant	Rio Madeira	22.30	6,500
Hydroelectric power plant	Estreito	2.3	1,087
Alternative Sources	PROINFA	9.4	2,341
Total		34.00	9,928

#### Main Projects until 2010

TYPE	PROJECT	Investment (R\$ bn)	POWER (MW)
Hydroelectric power plant	Belo Monte	6.60	5,681
Thermonuclear power plant	Angra 3	7.2	1,350
Transmission lines	Tucuruí-Manaus	3.4	-
Total		17.20	7,031

#### Forecasted Investments in Energy (R\$ bn)

2007	2008	2009	2010	2007-2010	2011	2012	2013	2014	Total
8.80	23.95	18.00	15.18	65.93	14.56	6.83	3.13	1.22	91.64



## PAC – Growth Acceleration Program

### Boosting Oil Production\*

- These investments will increase oil production in 40% up to 2010

Forecasted Investments (R\$ bn)

Action	Untill 2010	After 2010
Petroleum - Exploration and Production	93.4	100.2
Refinery, Transport and petrochemistry	45.2	31.7
Natural Gas	40.4	6.2
Renewable fuel	17.4	27.0
<b>Total</b>	<b>196.4</b>	<b>165.1</b>

\*Average production in 2007: 1.8 th barrels per day

### Railways

- More 2.500Km railways
  - Integrating northern and southern regions
  - Northeastern region railway

Forecasted Investments (R\$ bn)

Source	2007	2008-2010	Total
Budget	558	235	793
Private and Financing	1,108	5,962	7,070
<b>Total</b>	<b>1,666</b>	<b>6,197</b>	<b>7,863</b>

Source: National Treasury (COAPI)

### Civil Airports

- Investments of R\$ 3 bn from 2007 to 2010

Forecasted Investments (R\$ bn)

Source	2007	2008-2010	Total
INFRAERO	305	664	969
Budget	573	1,459	2,032
<b>Total</b>	<b>878</b>	<b>2,123</b>	<b>3,001</b>

### Highways and Ports

- Ports handle 90% of external commerce
- 56% of investments in Ports focus on their main bottleneck: increasing water
- 21% of investments in highways focus on concession, crowding in the private sector.

Forecasted Investments (R\$ bn)

Highway	34.20
Ports	1.70
<b>Total</b>	<b>35.90</b>



## 2008 Tax Reform

### Why is it necessary?

- Motivation: High compliance costs, low neutrality
  - High complexity: Too many taxes over the same base
  - High level of distortions and fiscal war
    - Cumulative taxes
    - Different ICMS (state-VAT) across the 27 Brazilian States and more than 40 rates.
  - Excessive taxation on payrolls: High costs for the private sector
- Brazil currently has the necessary condition to go for the reform, namely, *Fiscal Space*
- Technological changes: Electronic invoice system (SPED) will allow the government to reduce fiscal evasion and also to better calibrate the modeling parameters for economic policy purposes.



## 2008 Tax Reform

### Draft Law: 6 main goals

1. Simplify taxes: reduce bureaucracy and legislation
2. Eliminate Fiscal War
3. Correct distortions: increase efficiency and stimulate investments
4. Reduce the tax burden: gradually cut rates of the most distortive taxes, without affecting revenues
5. Improve regional development policy instruments
6. Improve the quality of cross-state interactions

### General Overview: Dual system to be gradually phased over 5 years

- Extinction of 5 Federal Taxes and creation of a Federal Value Added Tax (VAT-F)
  - To be implemented in the second year after legislative approval
- Extinction of 27 ICMS legislations and creation of a unified State Value Added Tax, a new ICMS
- Tax should be collected in the **final destination**, not in the original site, as we currently face.

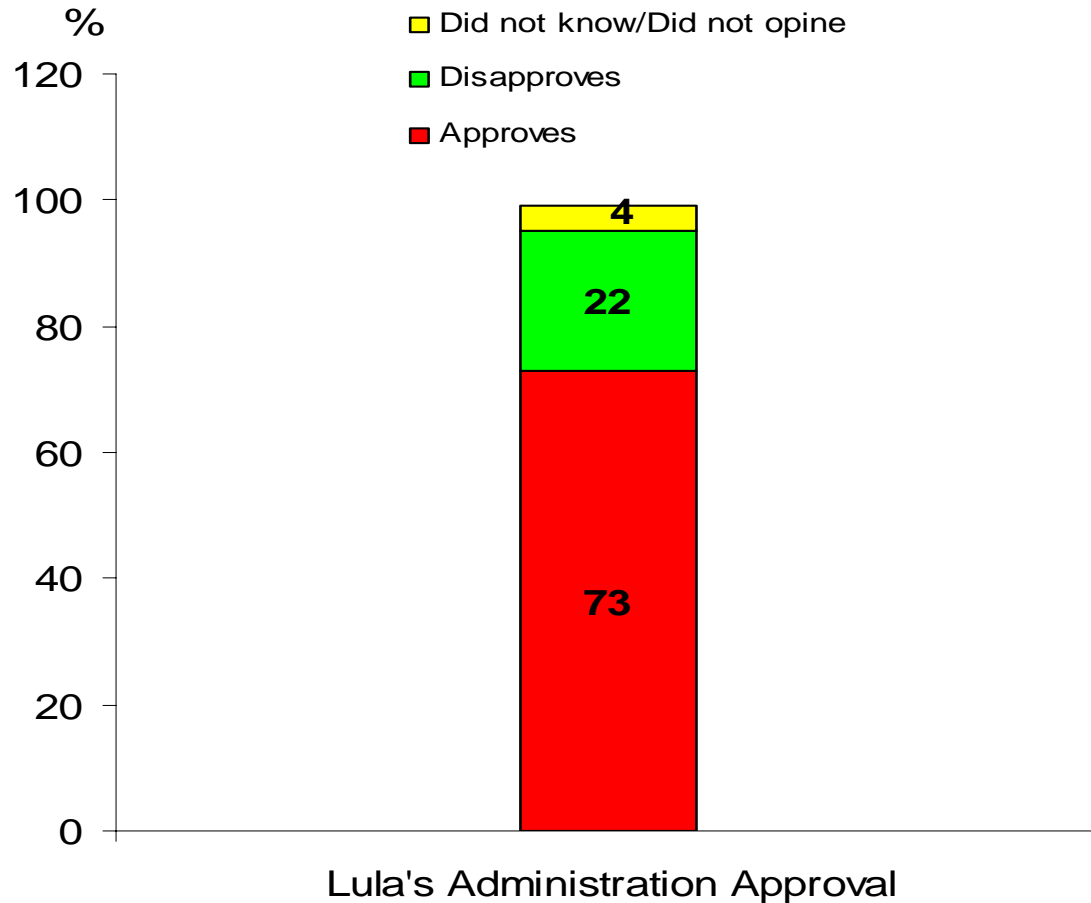


# POLITICAL SUPPORT



## POLITICAL STABILITY

- The index of positive results demonstrates improvement in the evaluation of President Lula's Administration\*



\*/ Survey at March/08.

Source: CNI/IBOPE



## ECONOMIC, GROWTH AND DEVELOPMENT POLICY

The immediate challenges faced by the Federal Government are:

- **Increase in infra-structure investments – PAC**
- Tax reform and simplification with reduction of the tax burden
- Reduction of the tax incidence on labor
- Social Security reform
- Political reform
- Education Development Plan
- Industrial Policy
- Export Acceleration Program
- Current expenditure control

