

## Brazil

The Brazilian economy slowed in 2011, growing by nearly 2.9% compared with 7.5% in 2010. The slowdown was attributable to the depletion of idle industrial capacity and the impact of policies aimed at containing the surge in domestic demand and the resulting inflationary pressures. In the third quarter, given the deteriorating international situation and the loss of momentum in the economy, macroeconomic policy was oriented towards maintaining growth, especially by lowering the interest rate and announcing, in early December, a reduction in taxes on some consumer goods and the relaxation of credit control measures. These new steps are expected to help ramp up growth in 2012, to about 3.5%.

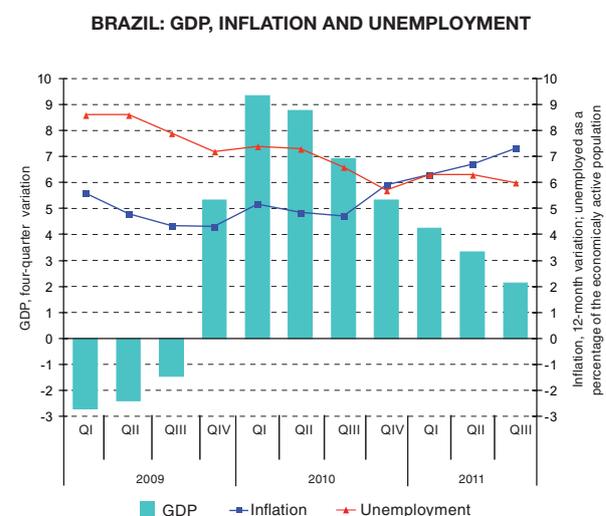
Fiscal policy was adjusted in 2011 to produce a primary surplus equivalent to 3.5% of GDP for January to October 2011, against 2.9% of GDP for the same period in 2010. The adjustment was in response to faster growth in federal government revenues (13.7% higher in real terms in the first 10 months of 2011 compared with the same period the previous year, excluding the impact of the sale of Petrobras concessions in 2010) and tighter controls on spending, with a real variation of 4.3% in the same period.

With regard to the variation in the two main taxes in the first 10 months of 2011, corporate tax revenues jumped by 17.6% in real terms and social security contributions went up by 9.4%. The 10 main federal taxes saw real increases in excess of 8%. The upswing is attributable chiefly to the real expansion of the wage bill and sales of goods and services. By sector, real tax revenues from mining doubled (117.6%) and federal taxes paid by the financial sector and the automotive industry climbed by 22.8% and 15.1%, respectively.

On the spending side, non-compulsory spending was reined in. Cumulative investment for the period January-October 2011 dropped by 8.7% in real terms compared with the same period in 2010. Expenditure was brought down in response to a review of projects and by monitoring and control of capital expenditure. The cumulative total for other capital expenditure grew by 4.9% in real terms—substantially less than in 2010, when it expanded by 16.6% in real terms. Staff costs and social security benefits (the two main expenditure

items) once again went up in real terms, by 3.7% and 4.7% respectively.

In early December 2011, the government announced a series of fiscal and credit measures to stimulate domestic production in response to the uncertainty caused by the international crisis. Taxes on household appliances, such as refrigerators and cookers, and certain food products, such as pasta, were lowered or eliminated. The tax on



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

foreign capital inflows for stock purchases and venture capital was eliminated, and the tax on personal credit transactions was cut from 3% to 2.5% per year.

Monetary policy was marked by an interest rate trend reversal. In the first half of the year, the central bank raised the Special System of Clearance and Custody (SELIC) interest rate from 10.75% in January to 12.5% in July, with a view to curbing inflationary pressures. In August that policy was changed as the central bank saw that the external situation was worsening. Between July and November the authorities lowered the SELIC rate to 11% and could lower it further in 2012. Credit expanded by 12.6% in the first 10 months of the year, slightly slower than the 16.9% recorded in 2010. However, lending patterns were influenced by macroprudential measures requiring financial institutions to hold more capital for longer-term operations.

Until the external situation deteriorated in August, Brazil's economic policy was concerned primarily with the constant inflow of capital; this led to the broadening of financial flow regulations. The financial transactions tax on loans and stock purchases was raised to 6% depending on the term of the operation, and a tax on trading in derivatives was announced. In view of the volatility since September, the government postponed implementation of some of these measures and recently stopped collecting some of these taxes on foreign investors.

The changing external situation resulted in exchange market volatility. The Brazilian real appreciated steadily between December 2010 and July 2011, by a nominal 6.7%, to give a rate of close to 1.50 reals to the dollar. With the deepening crisis in Europe, the Brazilian real was extremely volatile and saw sudden, small devaluations. Between September and November, the nominal exchange rate surpassed 1.90 reals per dollar and closed November at close to 1.81 reals to the dollar.

The 3.2% expansion of economic activity in the first quarters of 2011 marked a slowdown compared with the same period in 2010 and is attributable to the loss of momentum in various productive sectors. Agriculture grew by a slower 2.8% owing to the weak performance of the livestock sector, even though record harvests were expected for some of the main crops. Mining slowed dramatically and grew by only 3% as oil production posted a cumulative drop of 2% from January to September 2011 compared with the same period in 2010. Other minerals also expanded more slowly; one example is iron, which grew by 5.5% compared with 29.5% in 2010, according to the largest mining company in the country.

In the first three quarters of 2011, manufacturing grew by 1% compared with the same period in 2010. This loss of steam is attributable to flagging output of consumer goods (up by 0.4%) and intermediate goods (0.6% increase). The capital goods industry grew by

#### BRAZIL: MAIN ECONOMIC INDICATORS

	2009	2010	2011 <sup>a</sup>
<b>Annual growth rates</b>			
Gross domestic product	-0.3	7.5	2.9
Per capita gross domestic product	-1.2	6.6	2.0
Consumer prices	4.3	5.9	6.6 <sup>b</sup>
Real average wage <sup>c</sup>	1.3	2.1	1.3 <sup>d</sup>
Money (M1)	8.8	16.6	21.1 <sup>e</sup>
Real effective exchange rate <sup>f</sup>	1.5	-13.7	-6.2 <sup>g</sup>
Terms of trade	-2.4	16.0	8.5
<b>Annual average percentages</b>			
Urban unemployment rate	8.1	6.7	6.1 <sup>d</sup>
Central government overall balance / GDP	-3.5	-1.3	-2.0
Nominal deposit rate <sup>h</sup>	6.9	6.9	7.5 <sup>i</sup>
Nominal lending rate <sup>j</sup>	40.4	38.5	41.3 <sup>i</sup>
<b>Millions of dollars</b>			
Exports of goods and services	180 723	233 736	294 669
Imports of goods and services	174 679	244 322	304 948
Current account balance	-24 302	-47 365	-51 088
Capital and financial balance <sup>k</sup>	70 953	96 465	115 441
Overall balance	46 651	49 101	64 353

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

<sup>a</sup> Preliminary estimates.

<sup>b</sup> Twelve-month variation to November 2011.

<sup>c</sup> Workers covered by social and labour legislation, private sector.

<sup>d</sup> Estimate based on data from January to October.

<sup>e</sup> Twelve-month variation to October 2011.

<sup>f</sup> A negative rate indicates an appreciation of the currency in real terms.

<sup>g</sup> January to October average, year-on-year variation.

<sup>h</sup> Interest rate on savings.

<sup>i</sup> January-October average.

<sup>j</sup> Pre-set corporate rate.

<sup>k</sup> Includes errors and omissions.

5% during the same period. Slower growth in this sector can be explained by the impact of credit control measures and, especially, increasing competition from imported products.

In terms of the components of demand, domestic demand is expected to cool in 2011 compared with 2010. In the first three quarters of 2011, household consumption expanded more slowly (4.8%), as did government consumption (2.2%). Investment growth also decelerated over the year (5.7% compared with 21.8% in 2010). Sluggish domestic demand reflected the higher cost of credit, fewer new jobs and the effects of growing global economic uncertainty on domestic economic activity. One sign of cautiousness was the 28% fall in Brazilian Development Bank (BNDES) lending in the first three quarters of 2011 compared with the same period in 2010.

In November 2011 the 12-month variation in inflation was 6.6%. This is the first time that this indicator has gone down after rising continuously since September 2010, when it stood at 7.1%. The pressures exerted by food prices eased (falling from annual increments of nearly 10%, to 8.5%), but were substituted in part by those of fuel prices, whose 12-month rate rose from 2.5% in December 2010 to 6.5% in October 2011.

The average unemployment rate in the first 10 months of 2011 was 6.2%, almost 1 percentage point less than in 2010. During the same period in 2011, 2.2 million jobs were created. The real average wage increased by 3.4% in the 12 months to October 2011.

In the external sector, exports climbed by almost 30% in the period January-October 2011 compared with the same period a year earlier, maintaining the momentum seen in 2010. Imports continued to expand, but at a lower rate than exports: compared with the same period in 2010, their value increased by 25.5% in the period January-October 2011. This led to a 74.4% upsurge in the cumulative trade surplus for the period, bringing it to US\$ 25.4 billion. The wider trade surplus helped to offset the strong deflationary pressure of services in the Brazilian current account. The cumulative current-account deficit thus stood at US\$ 39 billion for the first 10 months of 2011; as a ratio of GDP it fell from 2.3% October 2010 to 1.8% in October 2011. With strong net inflows of capital, amounting to a cumulative US\$ 92.9 billion in the first 10 months of 2011, the central bank purchased foreign currency to bring international reserves to a total of US\$ 352.9 billion at the end of October 2011.

In 2011, service imports, income-balance deficits and expanding capital inflows towards Brazil maintained the upward trend seen over the past few years. There was a sharp increase in the cumulative services balance in the first 10 months of 2011 compared with the same period in 2010, as well as in the travel account deficit (which jumped by 45.2%, to US\$ 12.2 billion) and in

net remittances of profits and dividends (up by 26.6%, to US\$ 29.2 billion—similar to the US\$ 30.4 billion total for 2010).

Two significant foreign currency inflows were seen in the capital and financial account in the same period. Foreign direct investment shot up by 90.8% compared with the same period in 2010, to US\$ 56 billion. This increase is attributable both to the expansion in productive investments and to the change in capital position between Brazilian subsidiaries and their parent companies. Another source of foreign currency inflows was the larger volume of bank loans entering Brazil: net inflows totalled some US\$ 39.8 billion, representing an increase of 83.1%. These capital inflows partially replaced inflows for stock purchases, which dropped to US\$ 5.5 billion against the US\$ 33.7 billion in 2010 that mostly went towards the capitalization of Petrobras. On the back of the solid expansion in capital inflows, reserves were boosted by US\$ 56.9 billion —US\$ 13.6 billion more than in the same period in 2010.

Brazil's external debt went up in 2011. In October it stood at US\$ 297.8 billion, compared with US\$ 256.8 billion in December 2010. Long-term debt increased by US\$ 51.3 billion, while short-term debt decreased by US\$ 10.4 billion. Of that rise in long-term debt, 85.8% can be attributed to the banking sector, which used external borrowing facilities to support domestic operations. But the expansion in debt did not worsen the debt indicators, thanks to expanding reserves, burgeoning exports and falling international interest rates.