

BEST, JUNE 2007  
NEW YORK AND SAN FRANCISCO



## Brazilian Federal Public Debt - A Macroeconomic Overview



# Brazilian Federal Public Debt

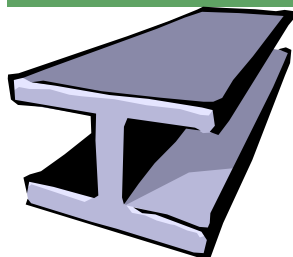
Macroeconomic Overview

Public Debt Management

## On the path to sustainable growth

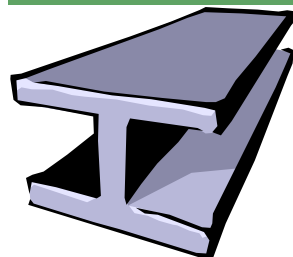
### The Economic Policy Mix Provides a Buffer Against External Shocks

#### Prudent Fiscal Policy



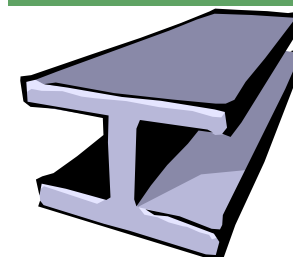
the main pillar of the economic policy

#### Cautious Monetary Policy



macro stability at the core of economic policies

#### External Adjustment



robust export growth and strong external accounts

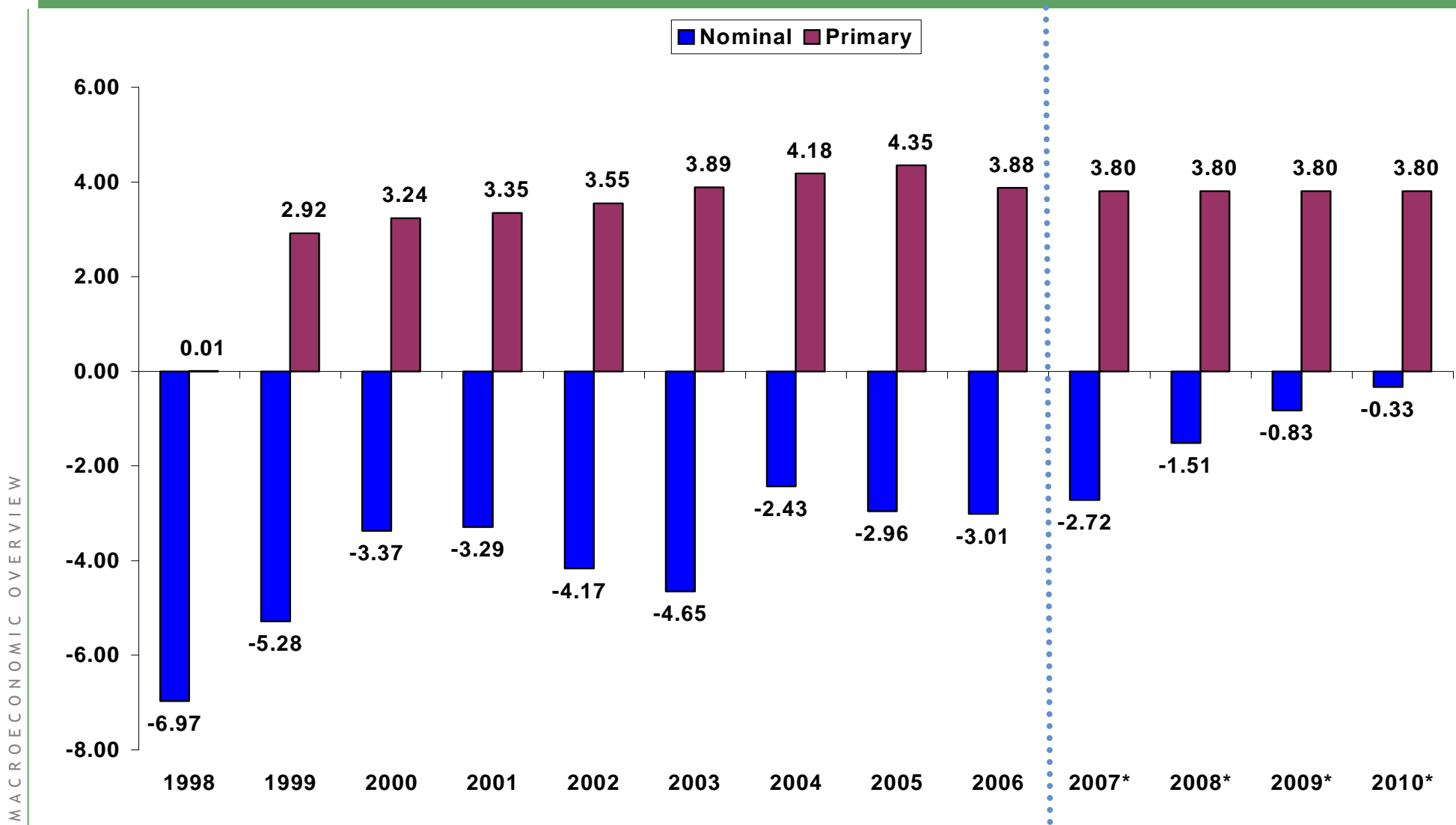
Lead to...

- ✓ Stable inflationary expectations
- ✓ Lower long-term interest rates
- ✓ Improved debt dynamics
- ✓ Greater fiscal flexibility
- ✓ More credit → more jobs

### Sustainable Economic Growth & Improving Social Conditions

# 1st Pillar - Fiscal Commitment

## Public Sector Balance (in 12 months)



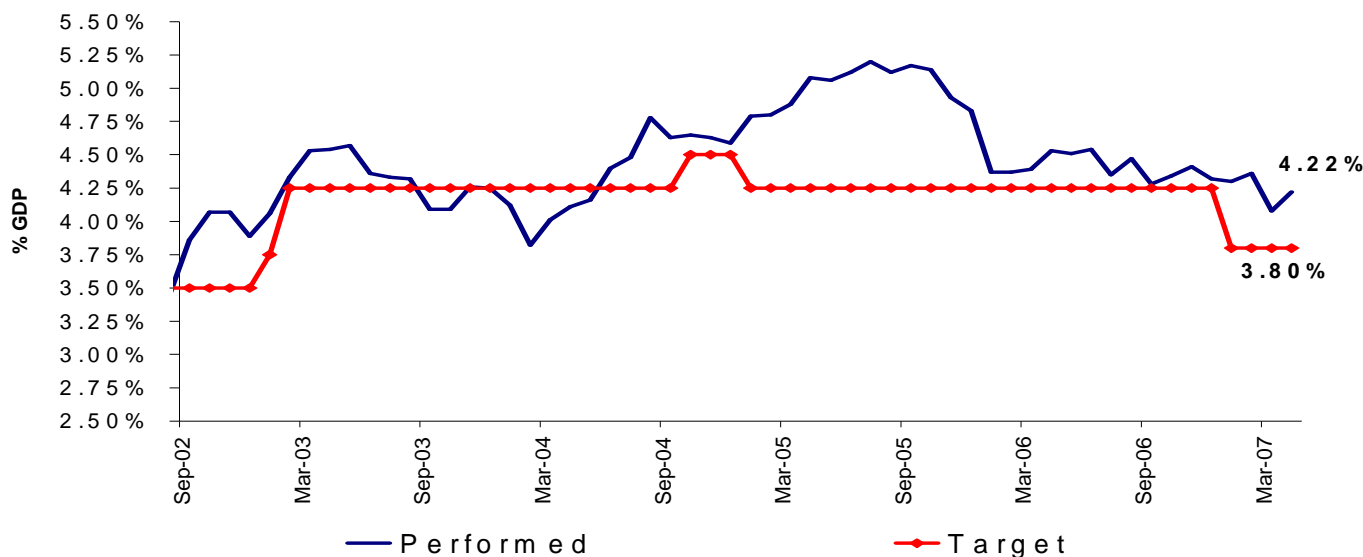
Source: Central Bank

\* Nominal Balance: Market Expectations; Primary Balance: Ministry of Finance

# 1st Pillar - Fiscal Commitment

## Keeping the Primary Balance for the next years

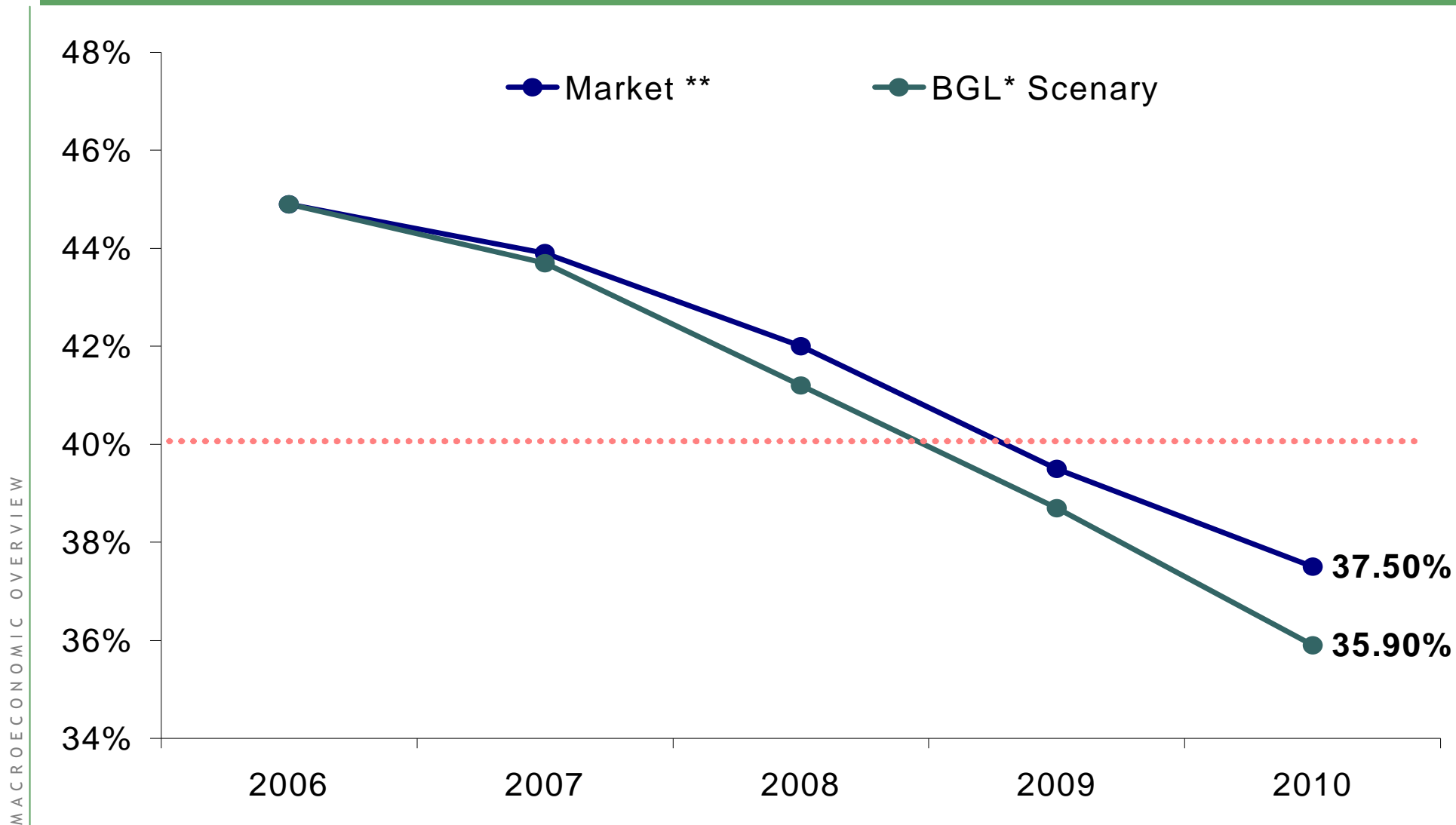
- **Budgetary Guidelines Law** - Already sent to the Legislative with the target
- **3.8% of GDP for the Primary Balance** - It corresponds to the same nominal fiscal effort that has been delivered prior to the GDP series revision.
- **0.45% of GDP regarding the PPI (Pilot Program for Investment)** - This is a cap to PPI, but still under rigorous criteria as for project selection.



Source: National Treasury

# 1st Pillar - Fiscal Commitment

## Net Debt / GDP scenarios based on market expectations

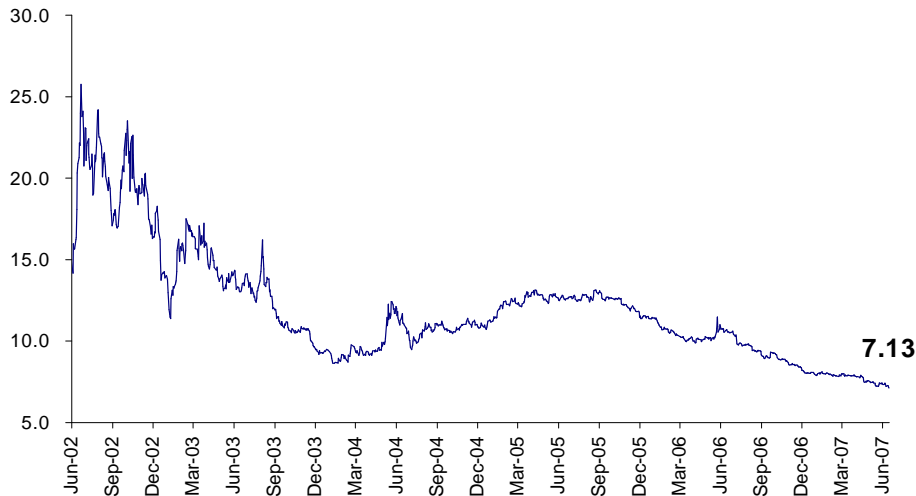


Source: National Treasury \* Budget Guidelines Law 2008 \*\* Central Bank/FOCUS 06/15/2007



## 2<sup>nd</sup> Pillar - Curbing Inflation drops real interest rate faster

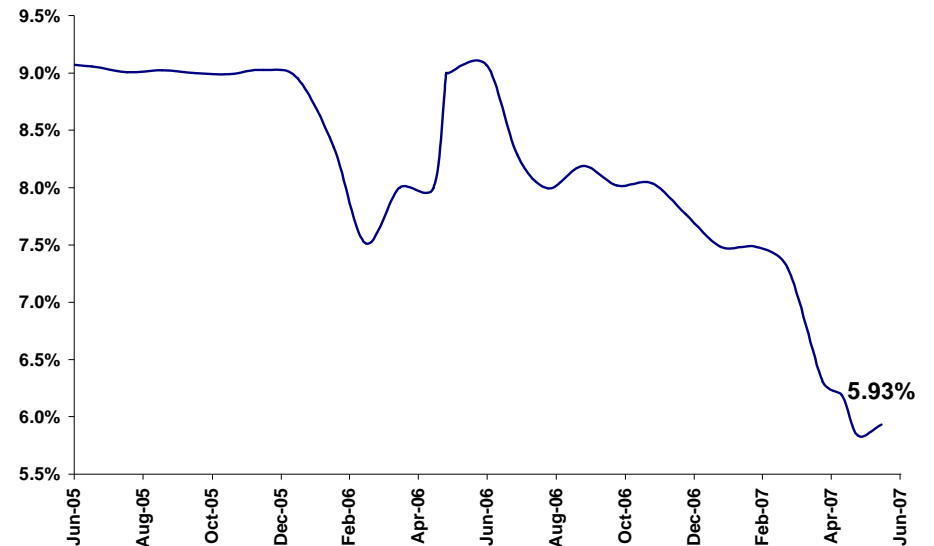
### Real Interest Rate (Swap 360 vs. 12-month CPI)



Source: Central Bank and Bloomberg

The improvement on economical conditions reduced dramatically the real interest rate on the short term from over 25% p.y. in 2002 to around 7% p.y. in 2007...

### Medium and Long Term Real Interest Rate on inflation linked bonds\* - Average rate of auctions



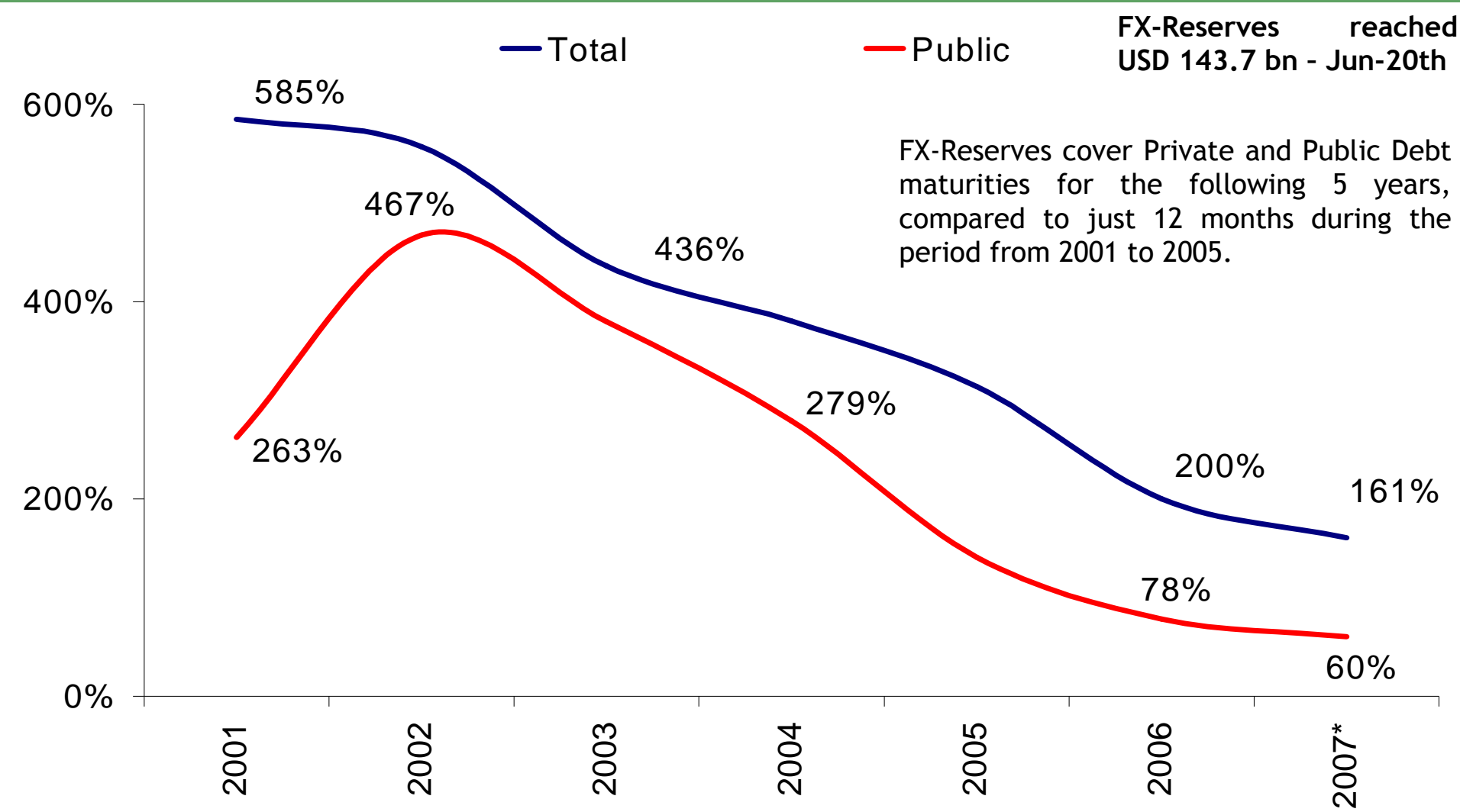
Source: National Treasury

\* NTN-B: CPI indexed bonds, maturing in 2024, 2035 and 2045.

...and also the medium and long term real interest rate that fell over 160 bps only in 2007.

### 3rd Pillar - Reduction in the External Vulnerability

#### External Debt / FX-Reserves (%)



MACROECONOMIC OVERVIEW

\* Until March, 2007  
Source: Reuters and Central Bank



## Market Expectations for 2007-2011

### Market Expectations -- Median of the Sample Collected by the Brazilian Central Bank

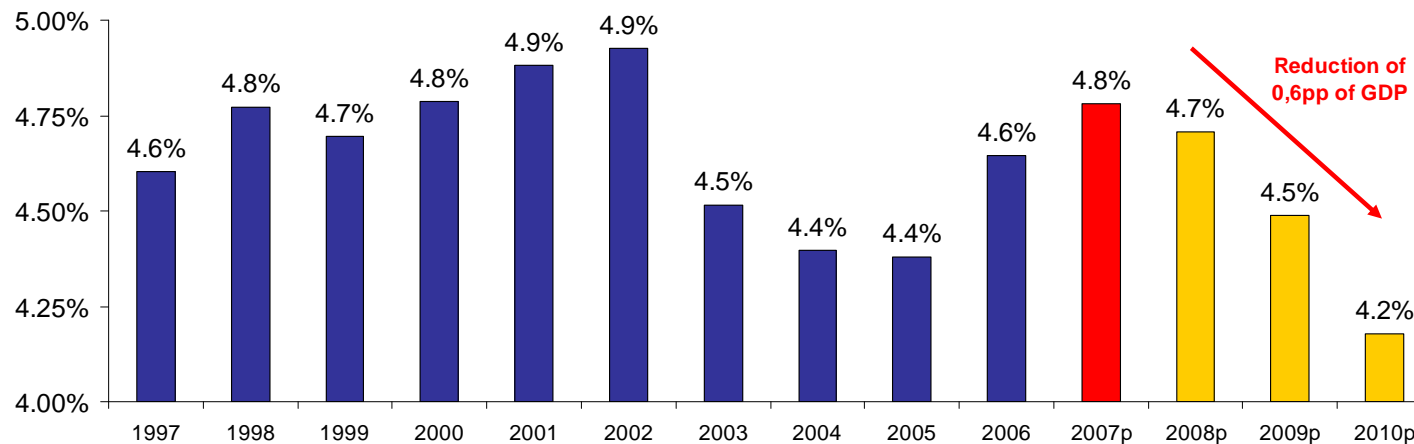
	Sample Date	2007	2008	2009	2010	2011
Primary Balance (% GDP)	12/30/2005	4.25	4.25	4.25	-	-
	06/15/2007	3.75	3.70	3.60	3.50	3.50
Trade Balance (US\$ billion)	12/30/2005	32.70	29.90	28.95	-	-
	06/15/2007	42.00	36.31	33.00	30.00	30.00
Current Account Balance (US\$ billion)	12/30/2005	3.16	1.00	0.00	-	-
	06/15/2007	10.00	5.00	0.00	-1.90	0.00
Exchange Rate Year End (R\$/US\$)	12/30/2005	2.55	2.68	2.80	2.63	-
	06/15/2007	1.93	2.00	2.10	2.16	2.20
Inflation (IPCA in %)	12/30/2005	4.50	4.50	4.50	-	-
	06/15/2007	3.59	4.00	4.00	4.00	4.00
Central Bank Average Interest Rate -- %	12/30/2005	14.53	13.38	12.50	11.78	-
	06/15/2007	11.84	10.25	9.55	9.10	9.00
GDP Growth (%)	12/30/2005	3.50	3.90	3.50	-	-
	06/15/2007	4.25	4.00	4.00	4.00	4.00
Foreign Direct Investment (US\$ billion)	12/30/2005	17.00	18.00	18.00	-	-
	06/15/2007	20.00	20.00	20.00	20.00	20.50
Net Public Sector Debt (% GDP)	12/30/2005	48.60	47.10	45.25	-	-
	06/15/2007	43.90	42.00	39.50	37.50	36.32

Source: Focus/Central Bank

## Capping Expenditures - A major concern

- Limit the growth of **personnel expenditures** of the Federal Government (ceiling = inflation + 1,5% per year).
- Create a **long-run policy for the minimum wage** (four-year policy - for 2008-2011: real growth rate = GDP growth of two years before).

Federal Government's Personnel Expenditures (% of GDP\*)



Source: Performed MF/STN  
p: Forecast MF/SPE

# Reforms in progress

Tax and Social Security Reforms - Will be sent to the Legislative on 2H-2007

## 1. Tax Reform

### *Recent Measures*

- ✓ Tax cuts to stimulate private investment, specially in **civil construction and infra-structure** projects.
- ✓ Tax cuts to stimulate the growth and formalization of **micro and small enterprises**.

### *Next Steps*

- ✓ Plan: unify the state VAT (ICMS) and the municipal service tax. **A federal VAT** would replace several existing federal taxes.
- ✓ By merging these into a federal VAT, the federal government would **simplify** the entire tax system

## 2. Social Security Reform

### *Recent Measures*

- ✓ Constitutional amendments<sup>1</sup> were a initial step to deal with the deficits

### *Next Steps*

- ✓ Social Security Forum: Created in Feb-07 and composed by the Federal Gov't, workers and employers representatives.
- ✓ It was designed to study and propose solutions for the Social Security system. **A proposal** is going to be sent to the Legislative in Aug-07.

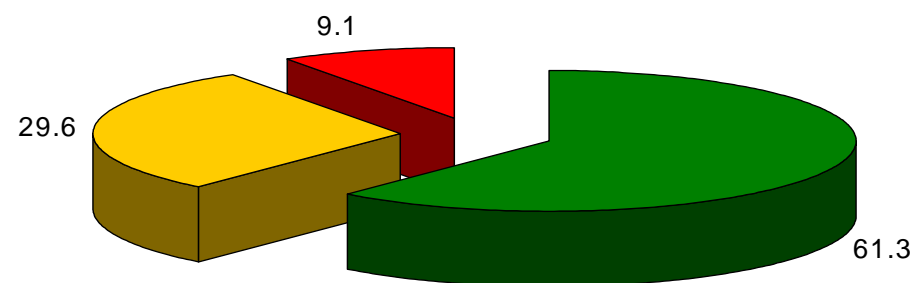
## Program of Growth Acceleration: 2007-2010

Investment - R\$ 503.9 bn forecasted for the next 4 years

- **Logistic:** 970 Actions/Projects => **69%** on the pipeline
  - Highways: 612 ongoing projects
- **Energy:** 459 Actions => **39%** on the pipeline
  - Electric power plants: 70 ongoing projects
- **Social and Urban Structure:** 217 Actions => **28%** on the pipeline
  - “Light for Everyone”: 26 ongoing projects

### Actions Performance - as % o Total Financial Programming

% of Actions Financial Programming



■ Adequate ■ Moderate ■ Delayed

Source: Presidency



## Brazilian investments on education - a long term project

### Education Development Plan

- The Education Development Plan investments reach R\$ 8 bn more than it was previously estimated for the Education Ministry until 2011;
- It sets some goals for public educational system:
  - Schools must achieve the same basic educational levels from OECD countries until 2022.
  - It establishes a floor for the teachers wages;
- The plan was built for all Brazilian educational system levels;



## What else are we building?

### Main achievements

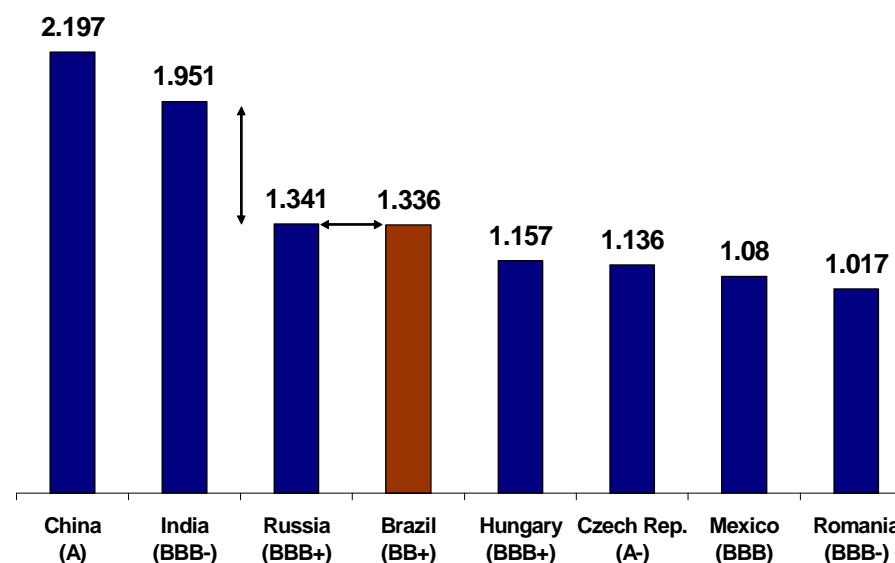
- Brazilian exports are diversified across countries and by products;
- Brazil is **self-sustainable in oil** since 2006;
- In 2006, roughly **45%** of Brazilian domestic energy supply came from **renewable sources**;
- Sugar cane ethanol - **top productivity in ethanol fuel**;
- Brazil has the 10th largest bond market in the world - USD 800 Bn (84% of GDP).
- Brazilian Stock Market Value reached 100.1% of GDP recently.

## What else are we building?

### Main achievements

- Social Inequality has dropped since 2001 and has reached its lowest historical level;
- Brazil has an equal or better business environment as most of its peers which already are investment grade.

### FDI Confidence Index



Source: A.T. Kearney - 2005

3 = high confidence



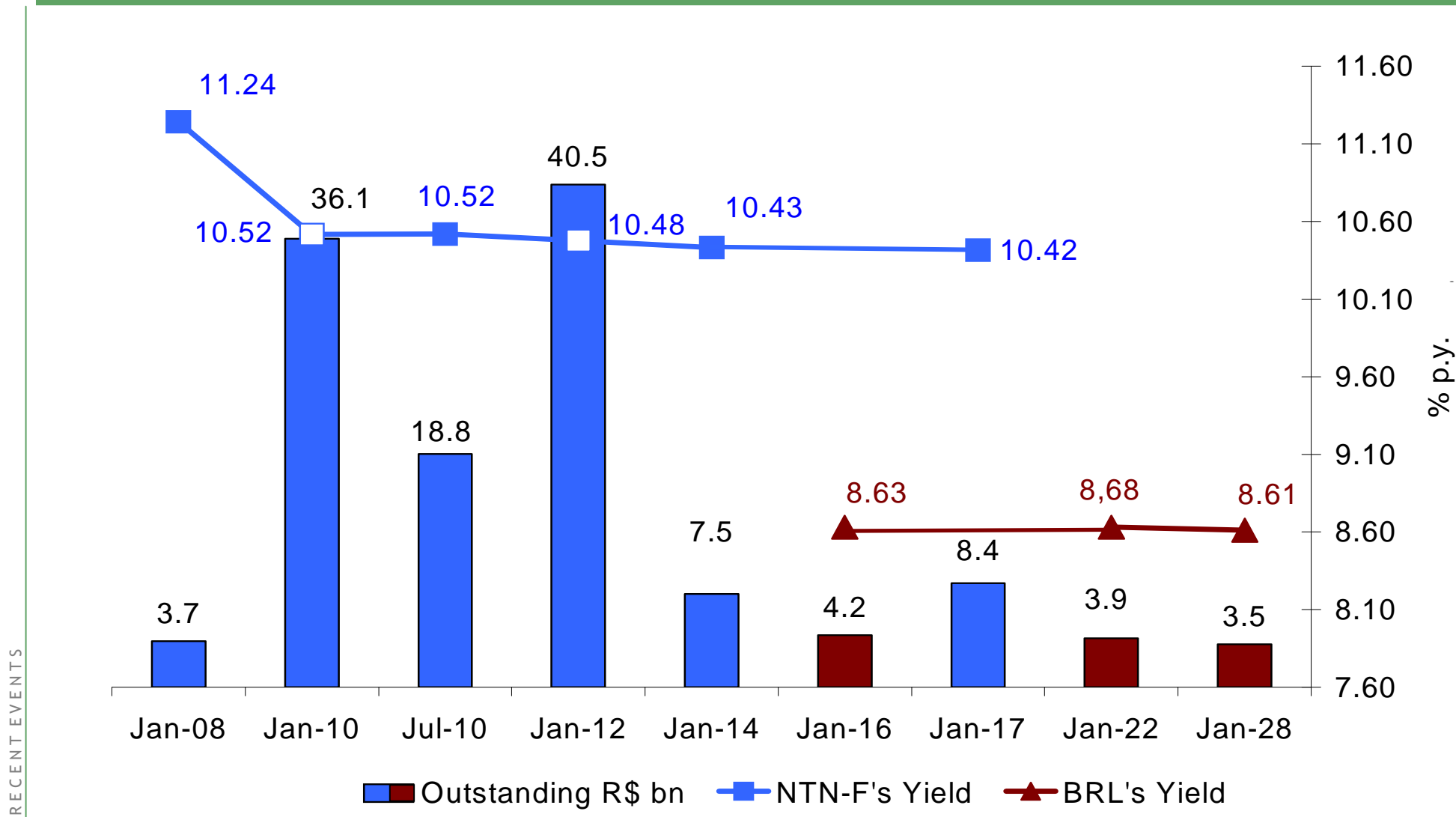
# Brazilian Federal Public Debt

Macroeconomic Overview

Public Debt Management

## National Treasury Performance - *Big opportunities merge in the domestic market*

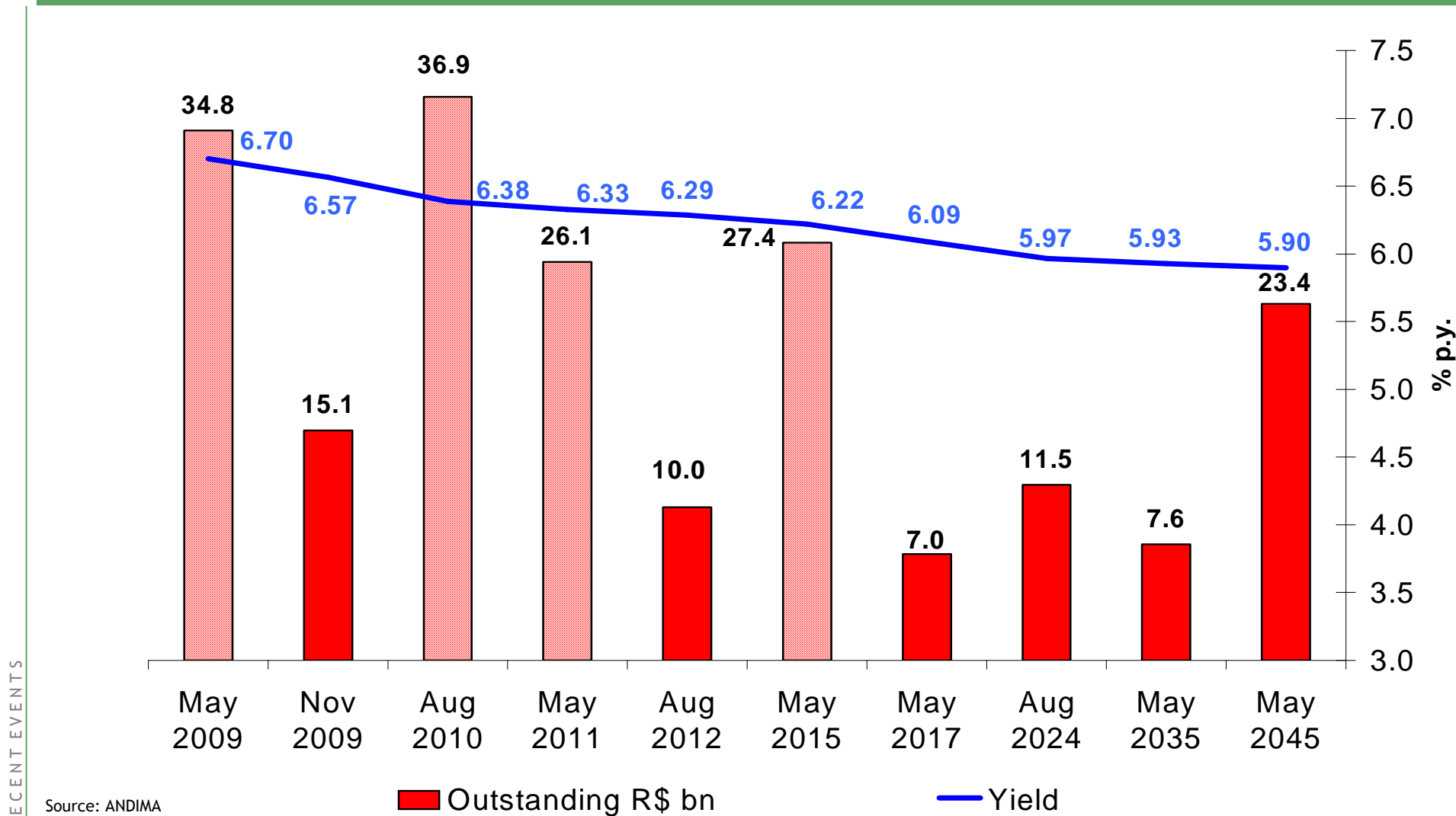
Domestic medium term fixed rated bonds (NTN-F) & Global BRL - Outstanding and yields (as of Jun-07)



Source: ANDIMA and Bloomberg

## National Treasury Performance - *Big opportunities merge in the domestic market*

Inflation linked bonds (NTN-B) - Outstanding and yields (as of Jun-07)



Source: ANDIMA

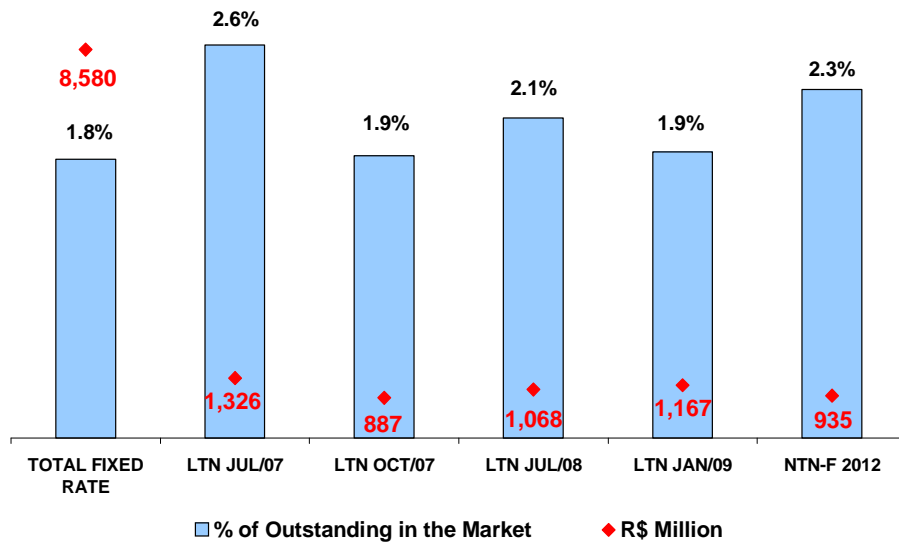
Note 1: The August 2010 NTN-B is not issued anymore.

Note 2: There are NTN-Bs with other maturities.

RECENT EVENTS

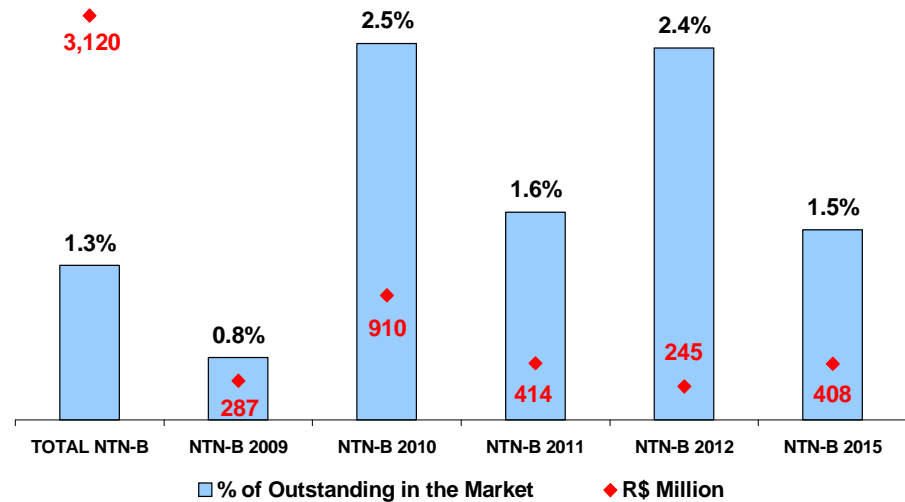
# Performance in Domestic Market - Liquidity Indicators

## Daily Turnover\* - Fixed Rate Bonds



Source: National Treasury \* as of May-07

## Daily Turnover\* - Inflation linked



Source: National Treasury \* as of May-07

### YIELD x Spread\* 06/20/07

	NTN-B 2010	NTN-B 2015	NTN-B 2045
Yield	6.38	6.22	5.89
Spread (bps)	8	5	7

	LTN JAN 08	LTN JAN 09	NTN-F 2012
Yield	11.23	10.62	10.47
Spread (bps)	4	4	8

\* The difference between Maximum and Minimum Rate from ANDIMA

## Next Steps

### Challenges

- Extending and consolidating both the foreign and the domestic: NTN-Fs and BRL curves;
- Providing more liquidity to the domestic market through dealers regulation;
- JCR (Japan Credit Rating Agency) placed Brazil as investment grade;
- Brazil is under rating revision by Moody's;
- According to the market, investment grade is expected in 2008 by the three main rating agencies.

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
<b>Moody's</b>	B1	B2	B2	B1	B1	B2	B2	B1	Ba3	Ba2	Ba2
<b>S &amp; P</b>	BB-	BB-	B+	B+	BB-	B+	B+	BB-	BB-	BB	BB+
<b>FITCH</b>	B+	B+	B	BB-	BB-	B	B+	BB-	BB-	BB	BB+



**For additional information access  
Brazilian National Treasury site:**

**[www.tesouro.fazenda.gov.br](http://www.tesouro.fazenda.gov.br)**

**Or contact Institutional Relations area:**

**[brazildebt@fazenda.gov.br](mailto:brazildebt@fazenda.gov.br)**

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