



**BANCO CENTRAL
DO BRASIL**

**XLIV Anual Meeting of the Asociación Argentina de
Economía Política**

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The Brazilian Reaction to the Financial Crisis

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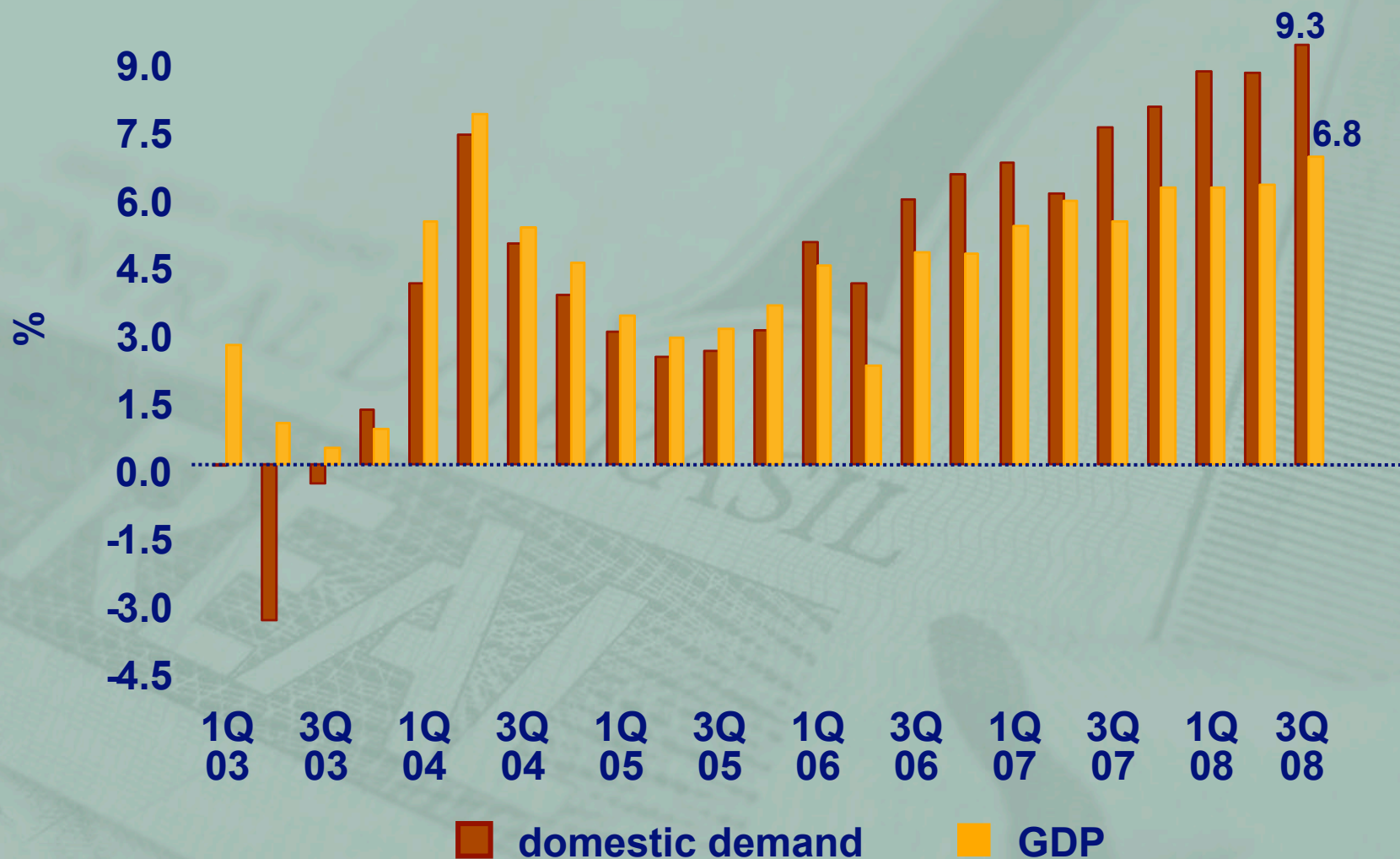
Outline

- **Brazil at the Outset of the Crisis**
- **Transmission of the Crisis**
- **Reaction to the Crisis**
- **Conclusions**

Brazil at the Outset of the Crisis

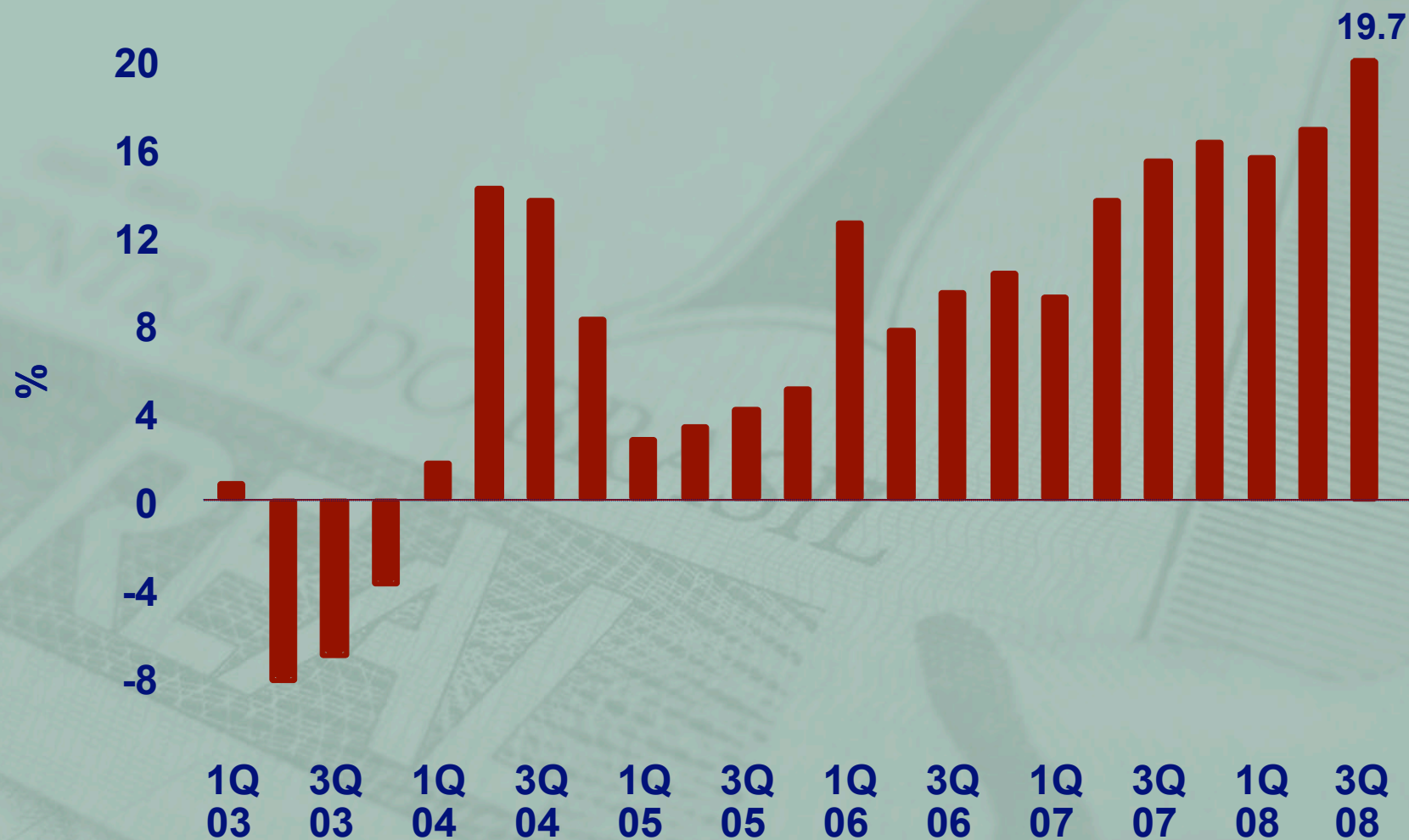
Domestic Demand and Supply

change year-over-year



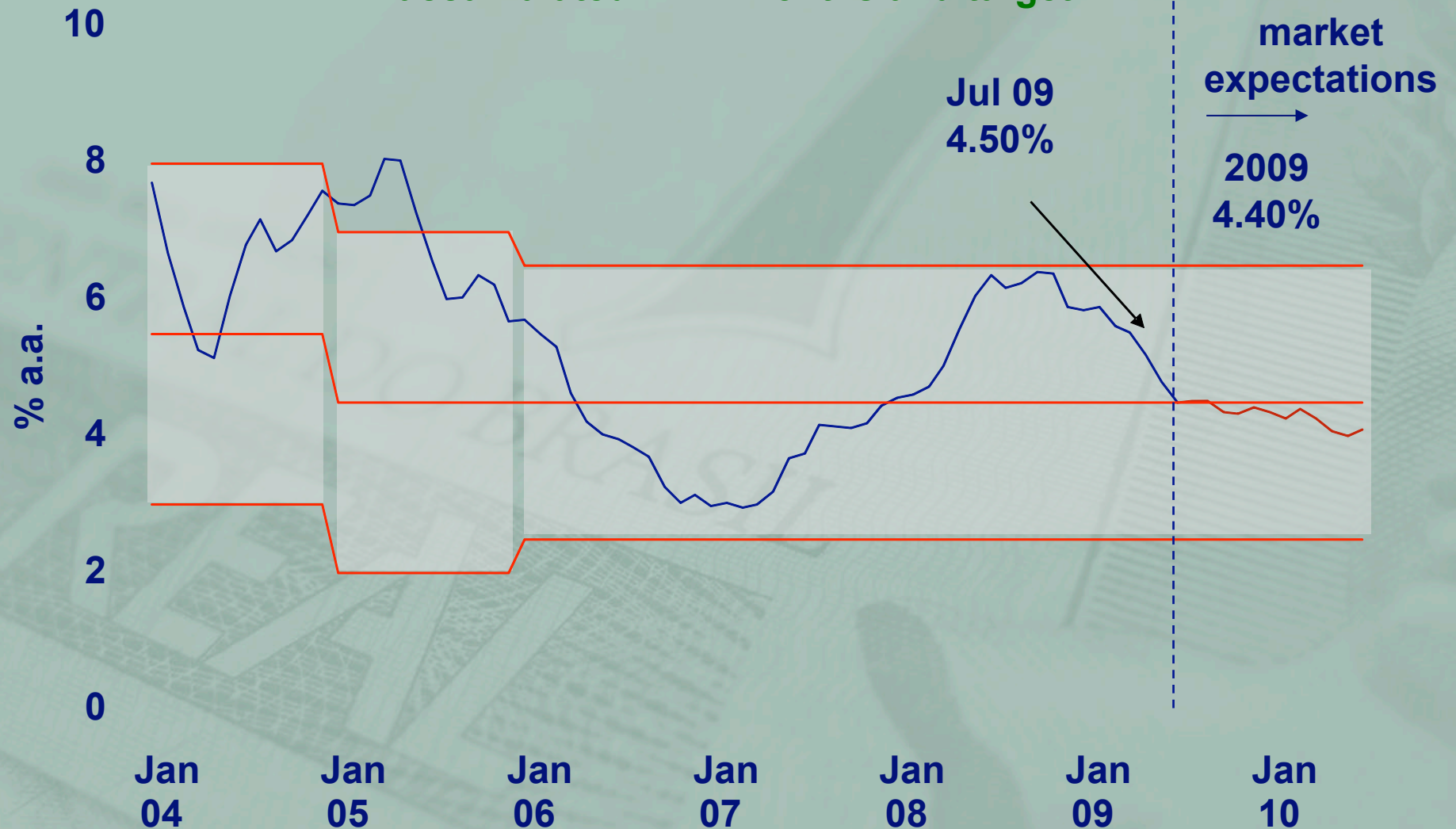
Fixed-Capital Investment

change year-over-year



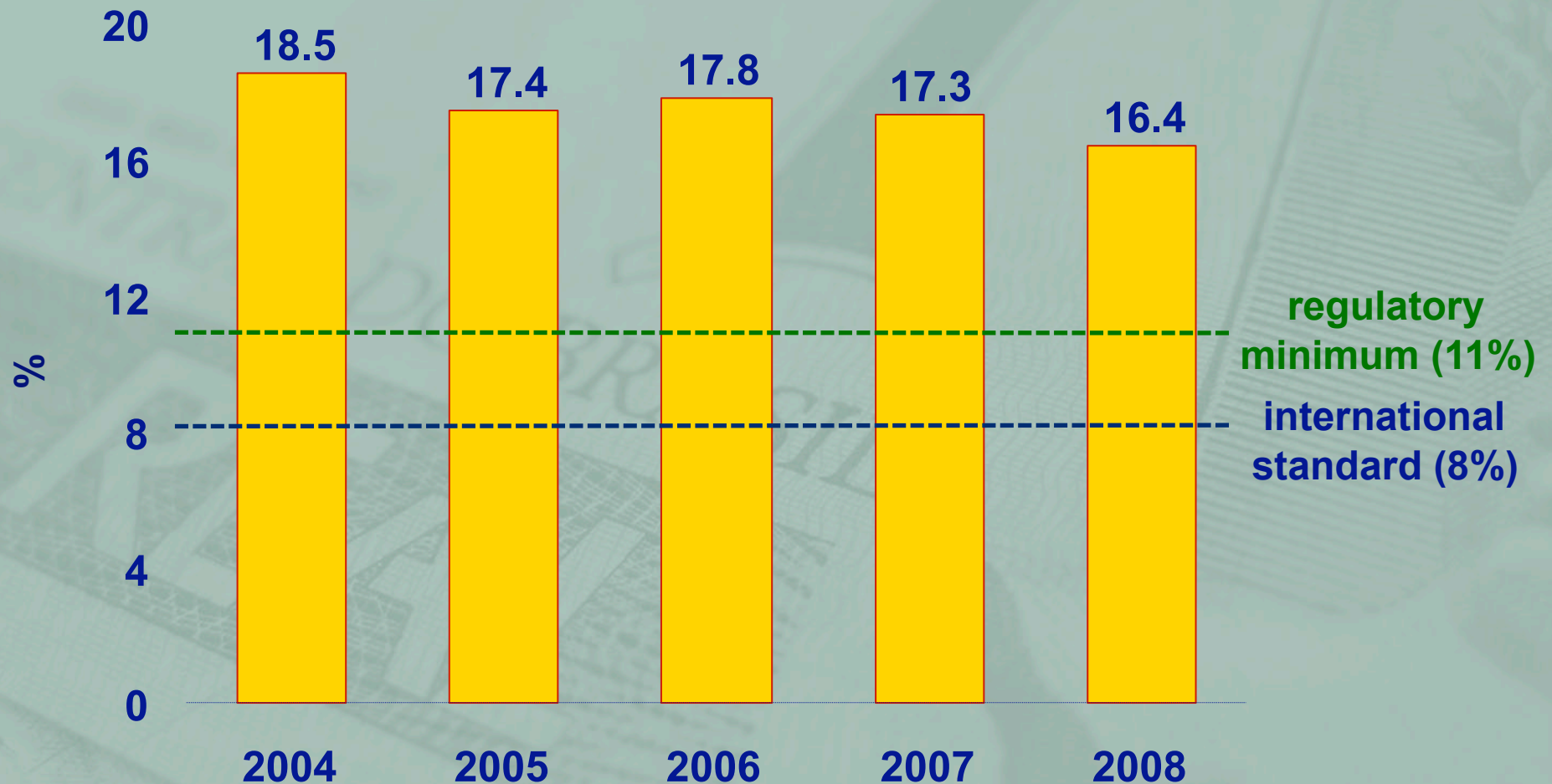
Inflation

IPCA accumulated in 12 months and target

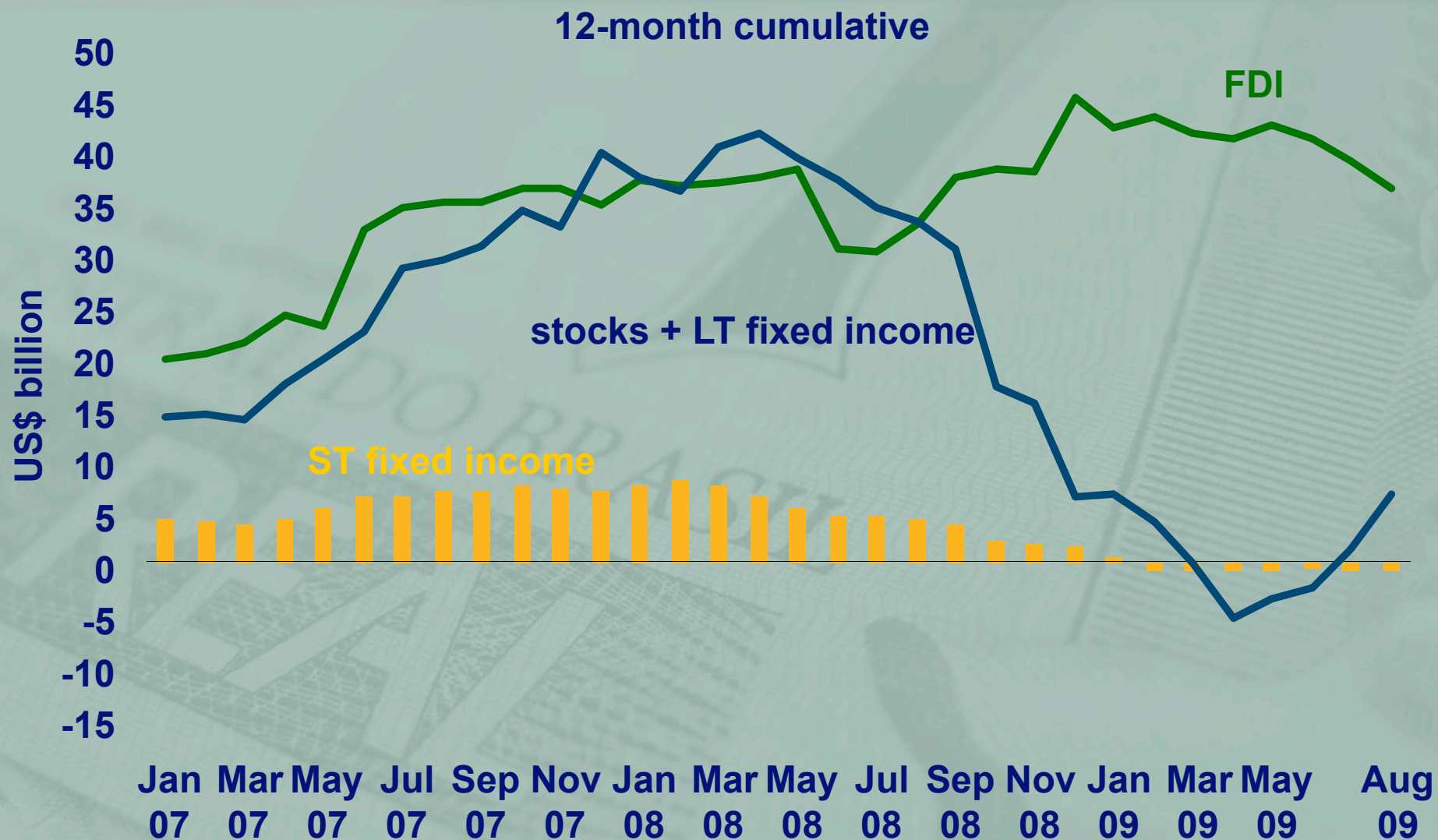


Bank-Capital Adequacy: Basel Index

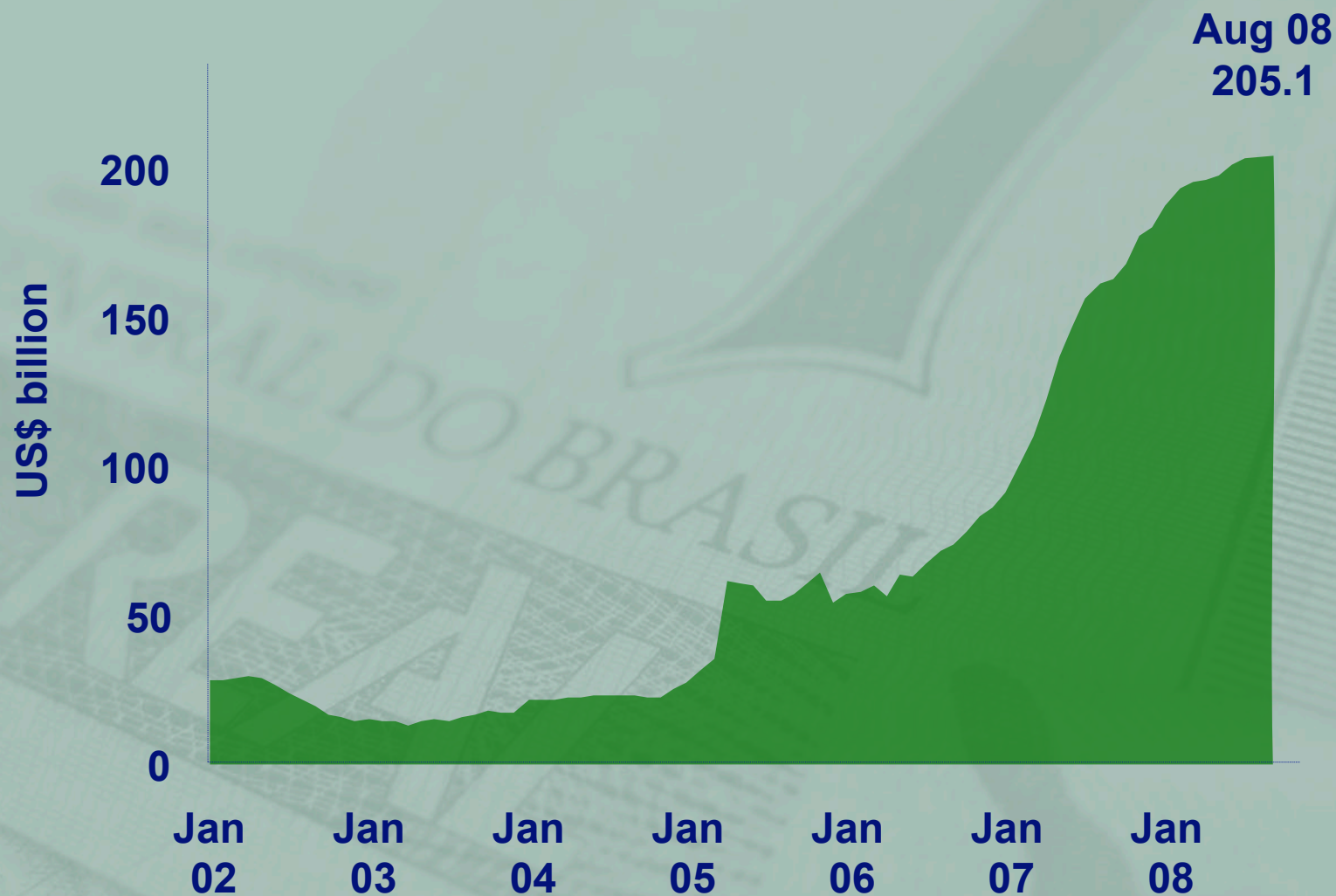
relation between capital and risk weighted assets



Net Foreign Investment – FDI x Stocks and Long Term Fixed Income (LT) x Short Term Fixed Income (ST)



International Reserves



Source: Central Bank of Brazil

Net Public External Debt



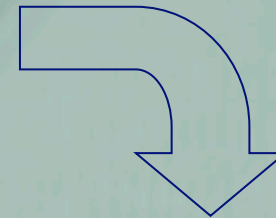
Source: Central Bank of Brazil

External Shock Feedback Loop: Now

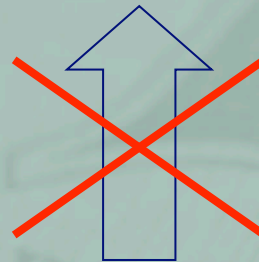
EXTERNAL SHOCK



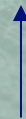
DETERIORATION OF CONFIDENCE



FX DEPRECIATION



REDUCTION OF PUBLIC DEBT/GDP RATIO



PUBLIC SECTOR IS LONG IN FX

~~FX PUBLIC DEBT~~

Transmission of the Crisis

Crisis – Transmission Channels



Credit



External Trade



Confidence

Credit Channel

SMALL BANKS

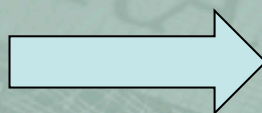
External Funding Cut
Loss of Deposits



Liquidity Squeeze (Local and FX)
Reduction in Credit-Supply

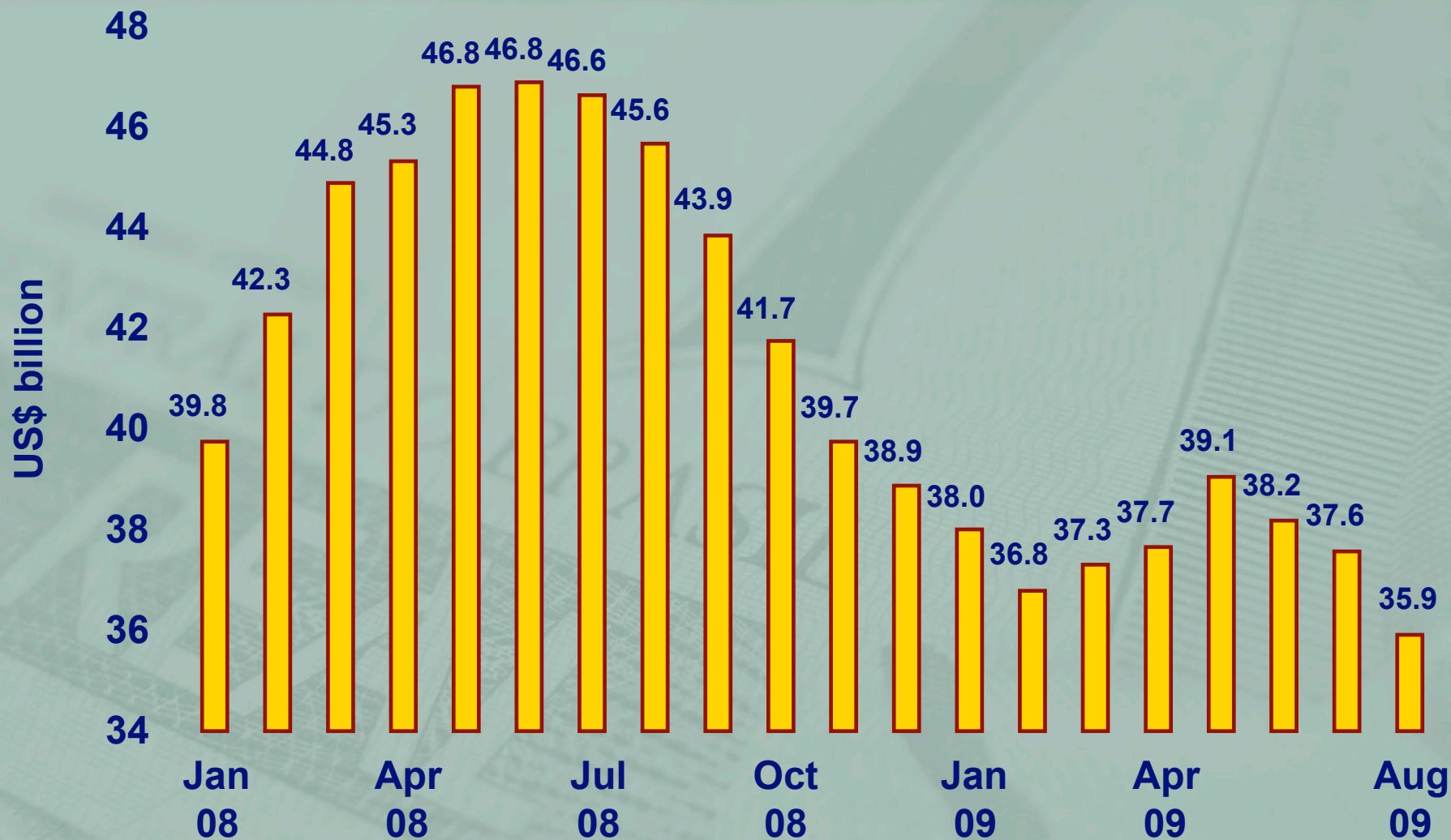
BIG CORPORATIONS

External Credit Cut
Loss in FX Derivatives



Demand for local sources
Recession in credit sensitive

Domestic Banking Credit with Foreign Funding

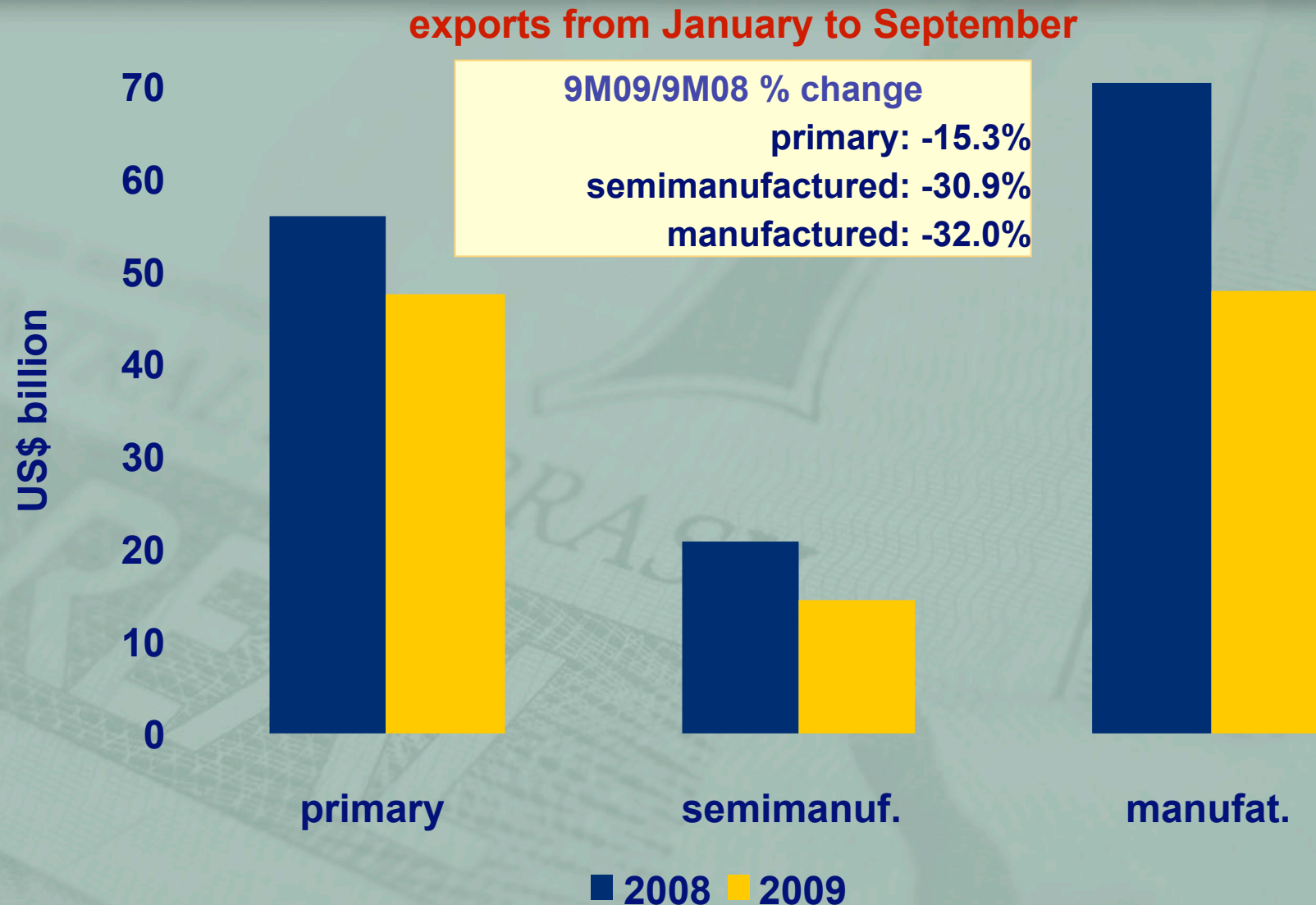


Stock of Banking-Credit to Big Corporations

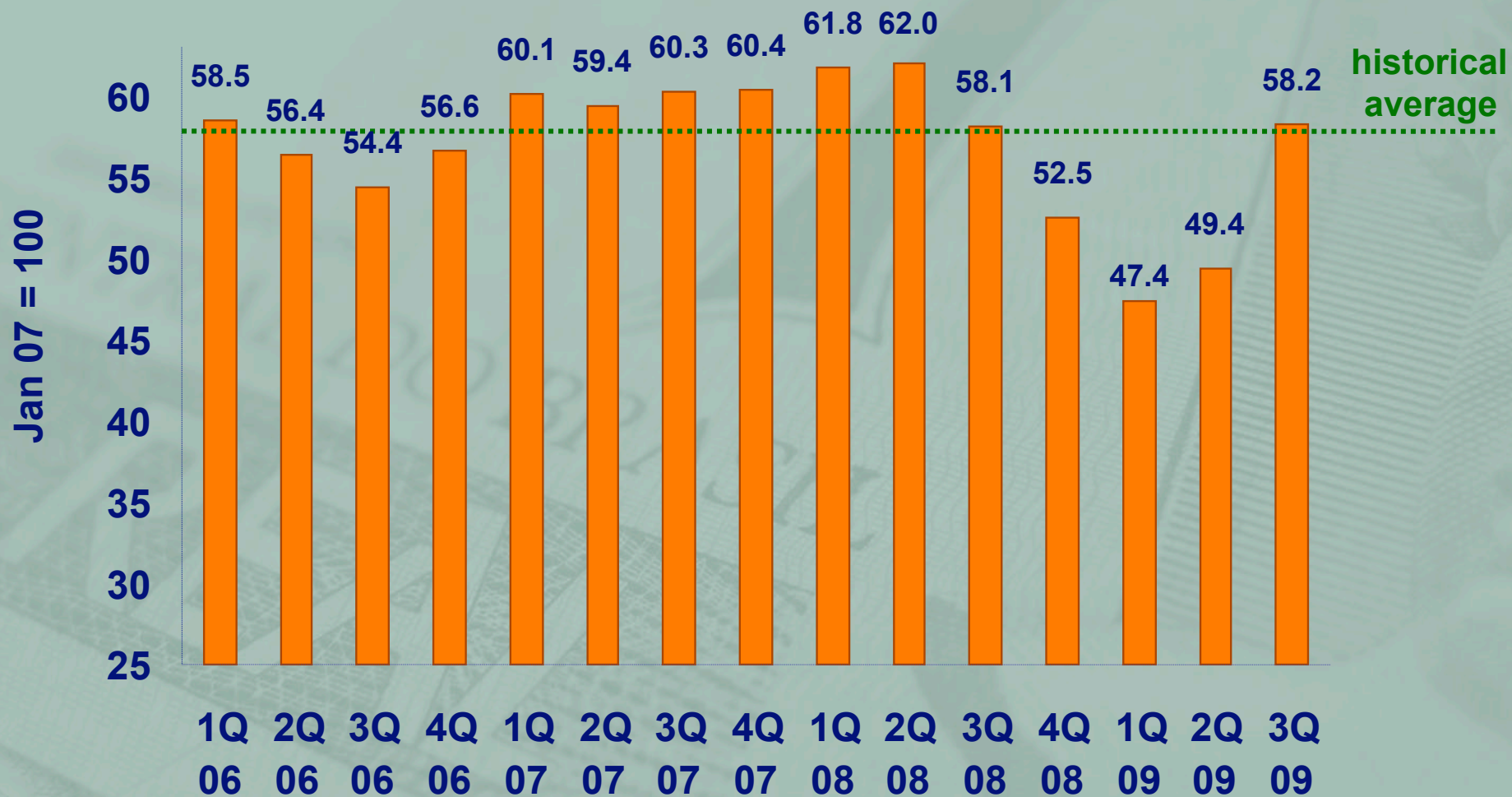
R\$ Billions



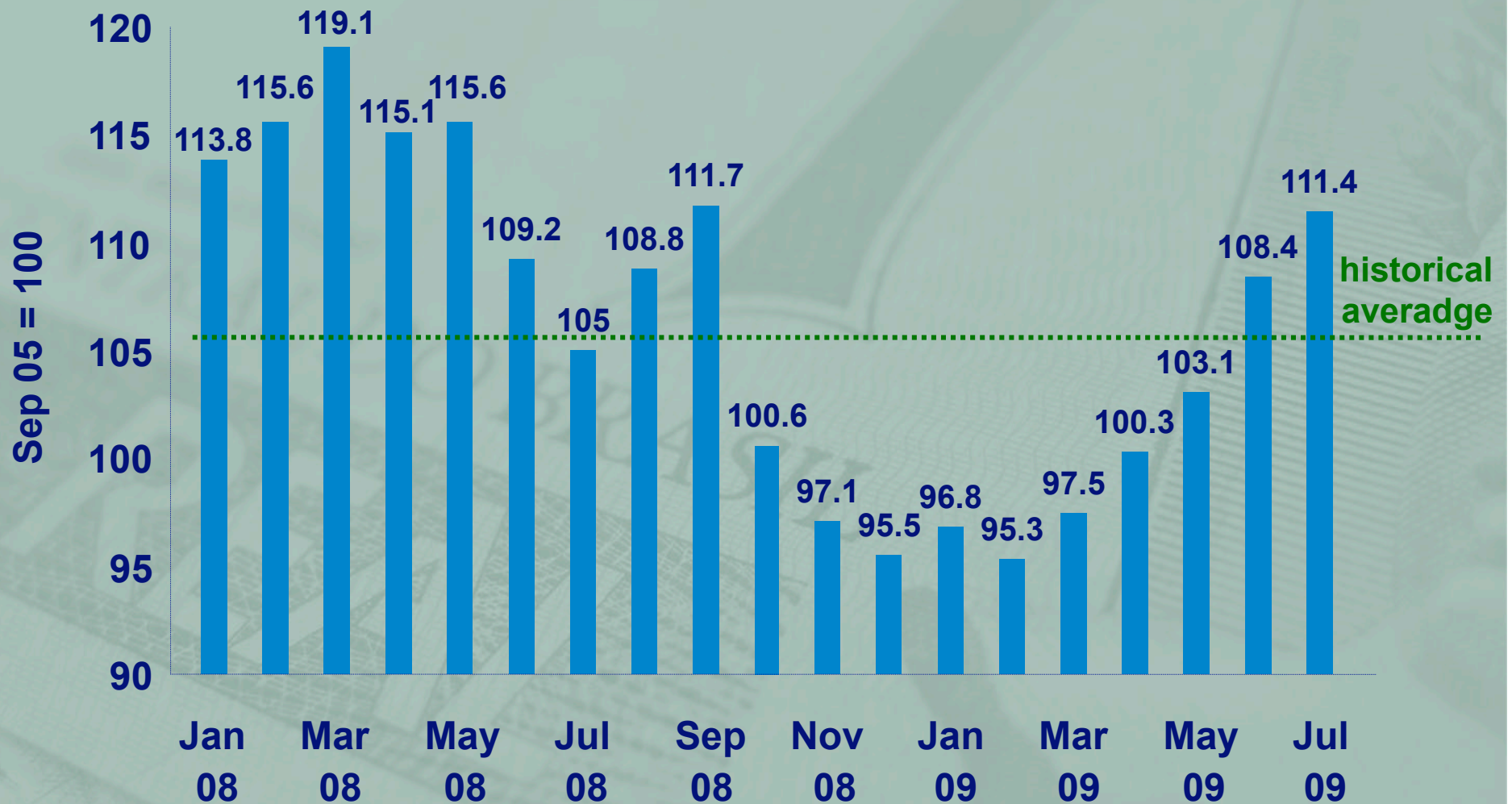
External Trade : Impact from the Financial Crisis



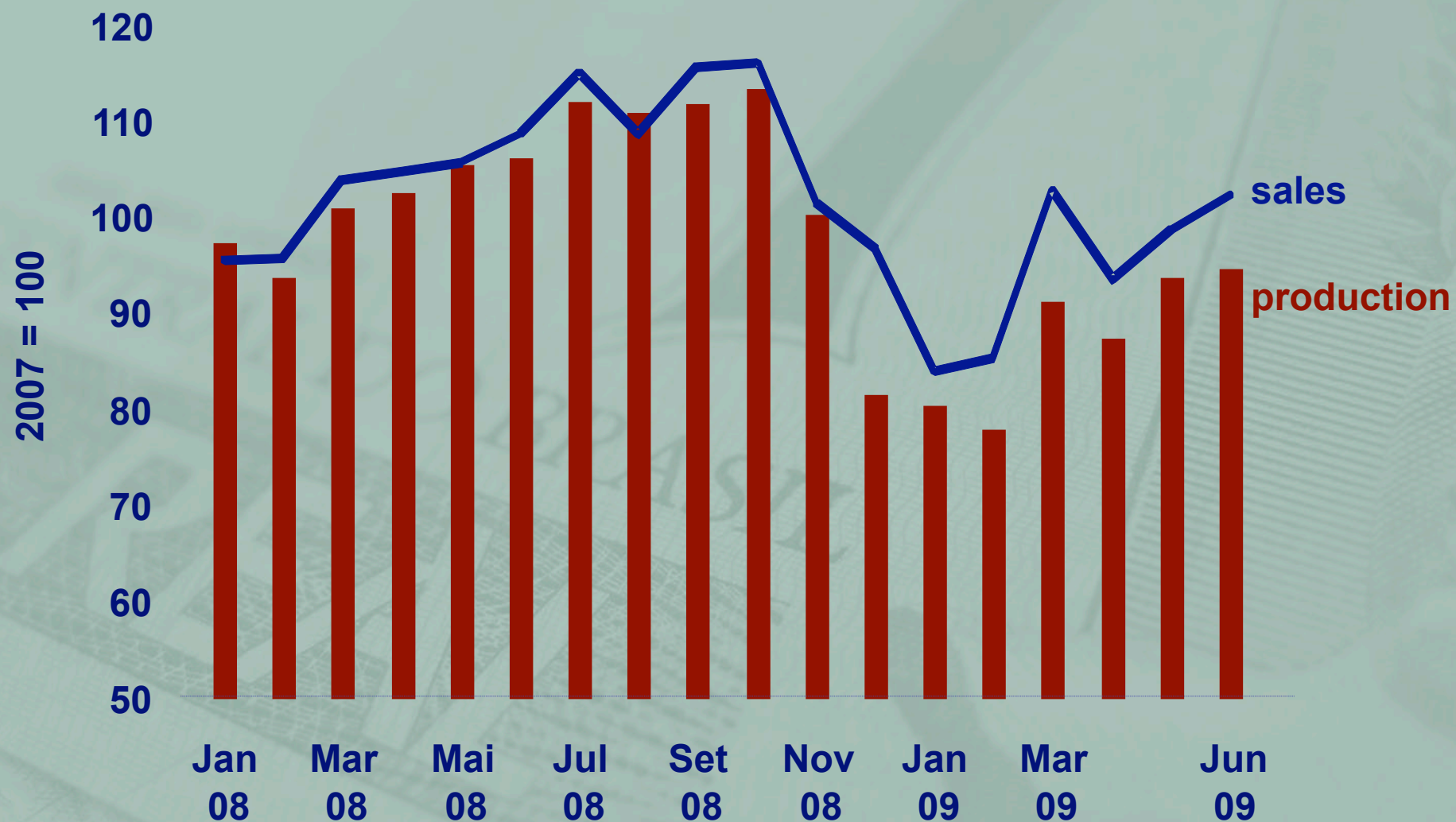
Industrial Confidence



Consumer Confidence



Industrial Production and Sales



Reaction to the Crisis

Overview of the Situation

- Collapse of international credit and interbank markets
- Extra demand on domestic credit market by firms that previously financed themselves in international markets
- Liquidity hoarding
- Credit quality deterioration due to exposure of non-financial big corporations to exchange rate derivatives



- Severe stress of small and medium financial institutions
- Severe credit restriction for exporters
- Credit tightening
- Recession in credit sensitive sectors, such as auto

General Perspective of the Reaction

- **Intervention in the local currency market**
 - **Aimed at providing liquidity to small and medium size banks**
 - **Without using public money**
- **Intervention in the FX market**
 - **Aimed at supporting exporters and providing liquidity to the market**
 - **Privileging loans rather than outright sales of foreign currency**

Anti-crisis Measures (CBB)

- **Liquidity injection in local currency**
 - **Compulsory reserves reduction**
 - **Incentives for big banks and the national private deposit insurance institution (FGC) to acquire portfolios of small and medium size banks**
 - **Authorization of banks issuance of Deposit Receipt with up to a R\$20 million guarantee by FGC**

Anti-crisis Measures (CBB)

- Initiatives in the FX market
- Liquidity injection
 - Auctions directed at exporters
 - Spot market sale of dollars
 - Sales of dollars in repo agreements
 - Exchange rate swaps auctions

Anti-crisis Measures (Other Institutions)

- Increase of funding to BNDES (Development Bank)
- The Federal Government pushed its banks to expand credit, partially smoothing the impact of retrenchment of private banks
- The Government announced a series of tax relief initiatives (auto, building), as well as outlay increases

Conclusions

- At the onset of the crisis the Brazilian economy was doing well and the perspectives pointed towards the continuation of that process
- Even though it was hit hardly by the crisis
- The transmission of the crisis materialized through credit, trade and confidence
- The reaction came through the provision of liquidity to the FX market (without a remarkable depletion of IR) and to the local currency market (with a sizeable reduction in RR)



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¡Muchas Gracias!