CNI ECONOMIC REPORT

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Adverse international scenario will slow down future economic growth pace

Performance of the real economy in 2008 was not affected by the international financial crisis

The Brazilian economy continues to perform at a remarkable level, as a result of a higher domestic demand. The worsening of the international financial crisis, however, changed the prospective scenario in two dimensions.

First, as difficulties increase, also affecting European countries, their immediate consequence is a lower international liquidity and fewer resources available to emerging economies, such as Brazil. Second, advanced economies will face economic recession, which will affect the dynamism of the international trade, regardless of all measures adopted to tackle the US crisis.

Brazil is in a better position to deal with these difficulties now than in the past: it has high reserves, a substantial primary surplus, a full-fledged bank regulation system and it is less dependent on foreign countries. However, this is not to say that Brazil is immune to the repercussions of the international crisis, even though its immediate effects are still quite moderate in the real economy.

Two main transmission vectors have been identified: a lower availability of international credit lines and a decline in foreign demand for Brazilian products. The first vector has a more immediate effect, while the second one will be progressively felt as global trade loses dynamism.

In the short run, the monetary authority should remain on the alert to detect liquidity problems and increases in credit costs, particularly in export credit costs. Non-renewal of foreign funding lines, combined with difficulties to fully replace them with domestic lines, makes it difficult to the corporations. Even if domestic inflationary pressures persist, it is also a must to reconsider the intensity of the current monetary policy, which was not designed to deal with a more adverse scenario such as the one prevailing right now.

A lower global economic growth will reduce foreign demand for Brazilians products, exposing Brazil's foreign accounts to a fragile situation and jeopardizing a major production-expanding factor. An increasing current account gap increases the need for foreign financing precisely when international liquidity is on the decline.

As foreign savings decrease, it is essential to enhance the domestic saving capacity to make sure investments continue to grow at the same pace. This requires higher public savings, which in turn imply a lower increase in current spending.

Thus, although the economy will grow by more than 5% in 2008, the new scenario is expected to bring about a turning point. The challenge for the Brazilian economy will be to ensure favorable conditions for economic growth in 2009 with the world economy growing at a much slower pace.

the Brazilian economy in the third quarter of 2008

Solid economic growth observed this year will not continue in 2009 — Page 2

Labor market sustains higher domestic demand — Page 4

Decline in commodity prices alleviates inflation pressures — Page 6

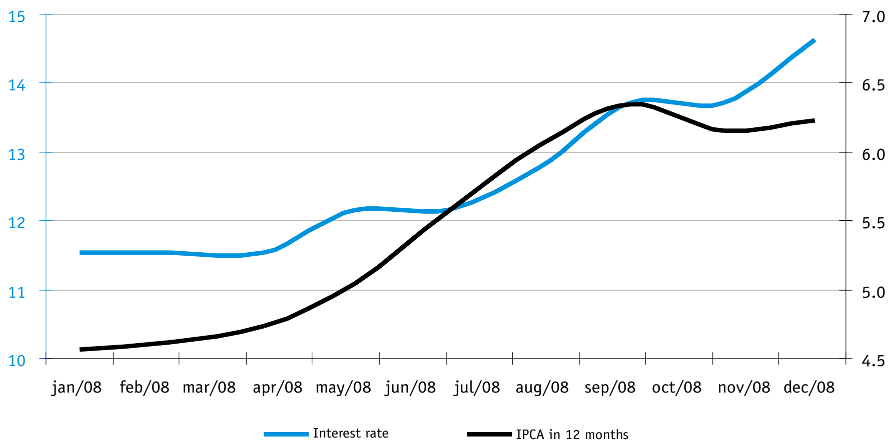
Higher spending reduces contribution of the fiscal policy to inflation control — Page 8

September was marked by uncertainties and changes in the exchange rate level — Page 10

Evolution of the Selic rate and expanded consumer price index

In 12 months (%)

Even if domestic inflationary pressures persist, it is also a must to reconsider the intensity of the current monetary policy



Source: Central Bank of Brazil and IBGE

Steady growth in 2008 will not continue in 2009

Monetary squeeze and financial crisis in the United States determine the economic activity future pace

The economic scenario in the third quarter is marked by duality: on the one hand, economic growth was remarkable in 2008 and, on the other hand, facts are emerging which foreshadow a turning point in this growth pace as interest rates rise and the financial crisis in the United States worsens.

GDP grew by 6.0% in the first half of 2008 in relation to the same period in the previous year. This growth is associated with a higher domestic demand, which increased by almost 8% in 2008 in relation to 2007. Demand, in turn, is fed by three factors: a higher real payroll and public spending and a greater availability of credit.

Real payroll is on the rise not only as a result of job generation, but also of a smaller inflation. Public spending has been growing at a faster pace since July. Finally, the share of credit in GDP increased in July and hit the mark of 38% of GDP in August, favoring both household consumption of more expensive products and investments, particularly in civil construction projects and in the purchase of machinery and equipment.

Domestic demand is fed by three factors

With income and credit on the rise, household consumption increased by 6.7% in 2008. Sales in the retail market increased at two-digit rates in the comparison between the averages observed in the first seven months of 2008 and 2007. More than consumption, economic growth is led by a higher investment rate. Gross formation of fixed capital grew by 15.7% in the first half of 2008 as compared to the same period in 2007. In the past two years – based on a comparison between the second quarters of 2008 and 2006 – gross formation increased by 32.3%. This is a growth pace that would make it possible for Brazil to double the volume of investments in five years.

A solid economic growth pace is guaranteed in 2008. However, while various indicators allow for a positive evaluation of the performance of the economy, there are increasing signs that this solid growth pace will not last long. The combination between interest rates on the rise in Brazil and the financial crisis in the US market is likely to lead to a lower growth scenario.

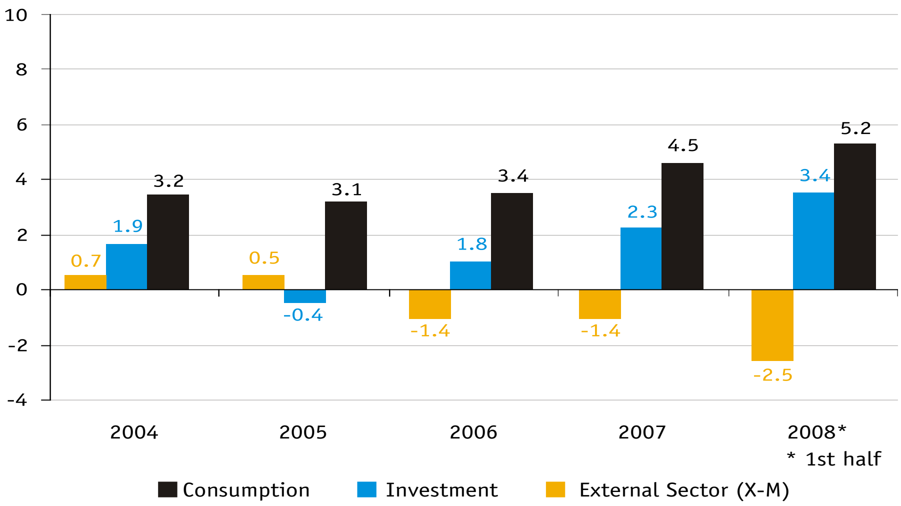
Growth of domestic demand will not dissipate quickly: it will take a while for the international financial crisis to affect production in Brazil. But the scenario anticipated for 2009 requires caution. The financial crisis will affect the Brazilian market through different factors: a) through retraction in international demand; b) through difficulties to access credit; c) through the loss of market value of Brazilian corporations; and d) through higher production costs, as the sudden appreciation of the US dollar will increase the cost of imported inputs, whose share in the productive process has increased.

Apart from the international crisis, economic growth in the last months of 2008 – and particularly in 2009 – will be hindered by sharper increases in interest rates. The monetary squeeze which began in April has not resulted in significant impacts on the economic growth pace in the second or third quarter. But the effects of the monetary squeeze, added to the effects of the international financial

GDP: Growth breakdown

In percentage points

Consumption and investment contribution to GDP growth is increasing on the last three years



Source: National Accounts / IBGE

crisis, are expected to be felt in the fourth quarter, slowing down the economic growth pace. This effect will be even more clearly perceived in 2009.

GDP is expected to grow by 5.3% in 2008

CNI has raised its estimate for GDP growth to 5.3% in 2008, virtually repeating the growth rate registered in 2007 (5.4%). This upward review of the economic growth pace – CNI's previous forecast was of a 4.7% growth rate in 2008 – was particularly based on the results of the National Accounts in the second quarter. The 6.1% GDP expansion observed in the second quarter of 2008 in relation to the same period in 2007 exceeded CNI's expectations, which were close to 5.5%. Aware of this fact, the outcomes of the manufacturing activity in this third quarter do not suggest any slowdown in this growth pace.

The industry is expected to grow by 5.5% in 2008, a little above the average for the economy at large. In the industry, the estimated growth of 8.7% in the civil construction sector deserves special mention. This growth is largely associated to a higher availability of credit for housing. The manufacturing industry – the largest segment of the industrial GDP – has been growing a little less than the average for the industry at large (5.1%).

In 2008, the agricultural/livestock production is expected to grow by 5.5%. The growth observed in the agricultural/livestock production was largely determined by the high prices of agricultural commodities since last year, when they were used as the basis for a decision to increase the planted area and, consequently, the harvest in 2008. Largely stimulated by trade and financial intermediation, the service industry is expected to grow by 4.8%. Taxes are estimated to rise by 7.3% in 2008.

As for domestic demand components, CNI estimates that household consumption will increase by 6.0% and account for 70% of all the economic growth in 2008. Government consumption is expected to increase by 5.6% in 2008.

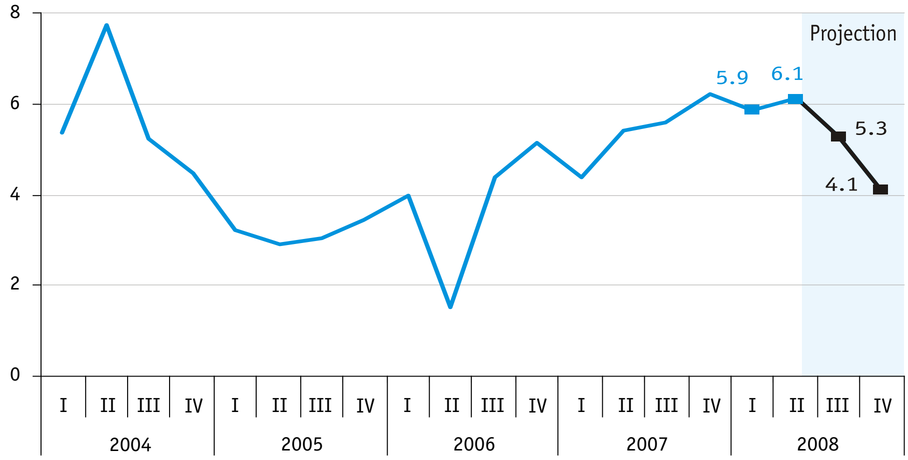
CNI has raised its estimate for the increase in the gross formation of fixed capital to 13.5%. This growth is associated to a more intense capacity utilization and to a higher public spending. The volume of exports of goods and services is expected to increase by 1.0% this year and imports are estimated to grow by 22.0%. As a result, the net contribution of the foreign trade sector to GDP formation is expected to be negative by 2.6 percentage points in 2008, close to the record figure of 3 percentage points registered in 1995.

The GDP growth pace observed in 2008 is not expected to continue in 2009. The impacts of interest rates on the rise and of the financial crisis in the United States are expected to restrict the economic activity after the fourth quarter of 2008 and more strongly in 2009, when the economic growth pace is expected to drop to about 3.5%.

GDP evolution

GDP: variation (%) in relation to the same quarter in the previous year

GDP growth may lose intensity during the second half of the year



Source: National Accounts / IBGE and CNI (projection)

GDP: Variation (%) in relation to the same quarter in the previous year

	june	july	august
Total	**5,73**	**1,54**	**-10,68**
Food and beverages	4,08	-0,56	-6,66
Energy (Petroleum, Gas and Coal)	7,56	2,09	-12,63
Industrial inputs	-1,33	1,05	-4,77
Agricultural Raw Materials	0,60	1,36	-0,18
Metallic Ores	-2,20	0,91	-6,90
Inflation Indices			
IGP-DI - General Price Index-Internal Availability	1,89	1,12	-0,38
Wholesale Price Index-Internal Availability	2,29	1,28	-0,80
IPC-DI - Consumer Price Index-Internal Availability	0,77	0,53	0,14
IPCA - Broad Consumer Price Index	0,74	0,53	0,28
Food Component of the Broad Consumer Price Index	2,11	1,05	-0,18

job and income

Labor market reduces unemployment at a faster pace

Jobs continue to be offered at a pace exceeding that of the demand for jobs

The labor market continued to increase the offer of new formal jobs throughout Brazil. More than 2 million registered jobs were created during the last 12-month period ending in August, which is a historical record (Caged, MTE).

Likewise, the data of the Monthly Job Survey (IBGE) – which covers the six main Brazilian metropolitan regions – show that both registered and not-registered jobs grew by 3.7% in August in relation to the same month in the previous year. This growth means that 771,000 new jobs were created during this period (more than the 623,000 jobs that were created last year).

Despite this intense growth in metropolitan jobs, the variation observed in August constituted the third consecutive slowdown as compared to the same month in the previous year: in May, jobs grew at a rate of 4.6%.

Changes were also observed in the growth trend of different metropolitan occupations. Registered jobs in the private sector, which grew by 9.1% in average in the first half of the year – in relation to the same period in 2007 –, registered lower growth in July (7.8%) and August (5.8%) as compared to the same month in the previous year. At the same time, not-registered jobs in the private sector followed an opposite path: after 13 consecutive months marked by a negative growth pace, they began to grow at a fast pace as of July of this year and hit the mark of 6.0% in August, also as compared to the same month in the previous year. Self-employment followed the same trend, but with a gap: their annual growth, which was losing momentum, picked up speed once again in August.

The combination of these movements interrupted a trend that had been observed for 42 months in a row: that of registered jobs in the private sector growing at a faster pace than non-registered jobs.

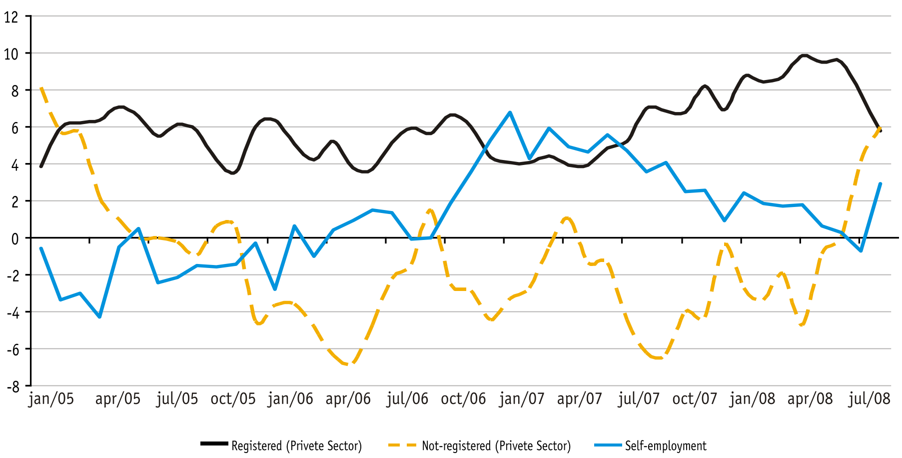
The formality index – which considers formal workers, the military and statutory servants in all jobs – revealed a greater supply of not-registered jobs and dropped for the third consecutive month (from 56.4% in April to 55.9% in August). It should be stressed that, despite this recent drop, this indicator is still 0.4 percentage points above the average registered in 2007.

The electoral period – due to the higher supply of informal and temporary jobs – might have influenced the drop observed in the formality index in the past three months.

Occupation variation, by type of occupation

Comparison with the same month of the previous year

Non-registered jobs is again growing in the same rate as registered jobs, after 42 months in a row



Source: PME/IBGE

Unemployment rate is expected to reduce drop pace

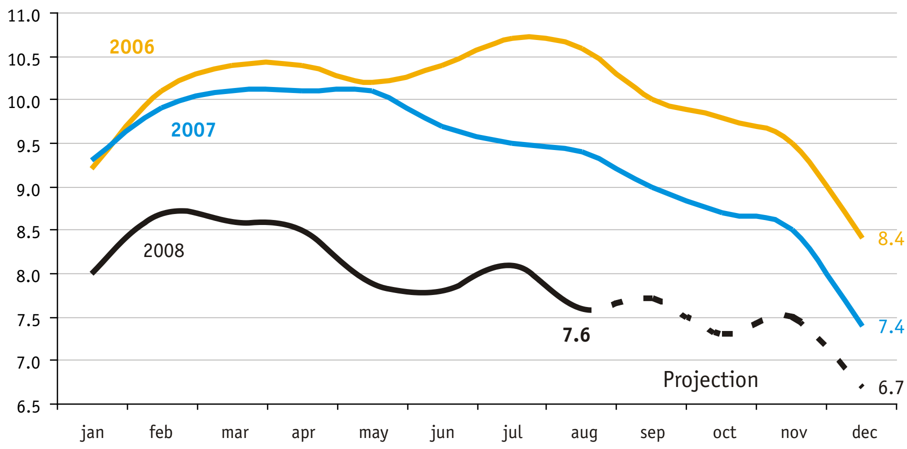
The unemployment rate began to drop months before the usual pattern observed in previous years. While in 2006 and 2007 the unemployment rate only began to drop in the middle of the second quarter, in 2008 it began to follow a downward trend in March. This movement continued until the unemployment rate hit the mark of 7.6% in August – the second lowest level since 2002.

This movement resulted not only from a high job growth pace, but also from a lower demand for jobs: since July 2007, jobs have been growing in relation to the same month in the previous year by at least 1 percentage point above the variation observed in the labor force. This gap increased in 2008 and exceeded 2.5 percentage points in May. In August, the growth gap of 2.2 percentage points resulted from an increase of 3.7% in the occupation rate and from a growth of only 1.5% in the labor force – both indicators in relation to the same month in the previous year. The income growth trend observed in recent years might be reducing the urgency with which secondary family members (such as spouses and children) are looking for a job to share household expenses, as was observed in 2003.

Unemployment Rate

In %

Difference between current unemployment rate and previous year figures will decrease until the end of 2008



Source: PME/IBGE

Positive wage negotiations guarantee higher income

Based on the result for August, CNI anticipates that the change of 1.8 percentage points in the unemployment rate in relation to the same month in the previous year will decrease progressively in the next few months due to a slower decrease in this indicator in the end of year. In December, due to seasonal factors, the unemployment rate will once again drop more sharply to 6.7%, which will be the lowest level registered for this indicator since 2002. As a result, the annual average of the unemployment rate will hit the mark of 7.9% in 2008.

Average real earnings usually earned by workers grew by 2.1% in August in relation to July. As compared to the same month in the previous year, the income growth rate increased more rapidly to 5.7%. This is the highest positive annual variation rate observed in the last 25 months, and it helps to explain the dynamism of domestic demand.

Wage negotiations have been playing a major role in the evolution of real earnings: 74% of all negotiations ensured salary increases above the inflation in the first half of 2008 (Dieese). The rapid drop observed in the unemployment rate is also creating pressures to increase proposed wages to attract the best applicants to available jobs.

Highest income growth was ensured by public servants and independent workers

Independent workers were the ones who enjoyed the highest increases in real income (12.3% in August in relation to the same month in the previous year), followed by public servants (10.3% in the same comparison). For the former, this high increase in earnings is explained by the fact that self-employed individuals enjoy greater flexibility to adjust their remuneration to price variations. For the latter, the increase in earnings resulted from collective bargaining with the government which led to salary increases much above the average granted by the private sector.

Total earnings are once again growing at a two-digit rate

Total earnings increased by 10.7% in real terms in August in relation to the same month in the previous year. This is the second highest variation on this comparison basis since 2002. A high occupation growth rate and a marked increase in the real income influenced this outcome. However, if the occupation rate continues to slow down – a possibility that is yet to be confirmed – it may reduce the growth pace of total earnings, particularly along 2009, when a lower economic growth pace is anticipated.

inflation, interest rates and credit

Decline in commodity prices eases inflation pressures

IPCA will remain close to the upper limit of the inflation target in 2008

The main pressure pushing the world inflation up lost momentum as international commodity prices dropped. Food and energy prices (considering petroleum, gas and coal) dropped by 6.7% and 12.6%, respectively, in August (IMF) in relation to the previous month. This behavior was caused by the worsening of the US crisis, as a result of which the global economy is expected to grow less (mainly the US economy).

The downward trend observed in commodity prices brought about almost immediate impacts on price indices in Brazil. Inflation in the wholesale (IPA-DI - Wholesale Price Index-Internal Availability/ FGV), whose variations in May and June exceeded 2%, increased less intensely in July and was negative in August (-0.80%). In September, although there was no deflation, the IGP-M (General Market Price Index) was virtually stable (0.1%).

As for the inflation rate for consumers, cost reductions were almost instantly transferred to prices. The food component of the IPCA (IBGE), which accounted for half the inflation registered in the past 12 months, was marked by deflation in August (in the variation in relation to the previous month). This movement was sufficient for the IPCA accumulated in 12 months to interrupt its acceleration trend – which had been registered for nine months in a row – and hit the mark of 6.2% in August (as compared to 6.4% in the previous month).

The rapid transmission of the effects of lower commodity prices to the domestic inflation confirms that most inflation pressures experienced in Brazil in the last 12 months were caused by external factors.

However, the recent decline in the inflation rate is still concentrated in food prices. The service component of the IPCA and the core inflation (excluding food and monitored prices) are still rising at a fast pace: both indicators increased by 5.9% in the 12-month period ending in August.

CNI projects that the IPCA accumulated in 12 months will once again rise slightly this year and that it will only lose momentum in December, closing the year at 6.2%.

Two factors influenced – in opposite directions – the behavior of the current inflation and, consequently, the projections for 2008. On the one hand, the effects of the decompression of international commodity prices were transmitted to inflation indices more fastly and intensely than expected. On the other hand, domestic demand continued to grow steadily. The slow pace at which the creation of new jobs in metropolitan areas lost momentum since the second quarter of this year has not impacted domestic consumption significantly so far. The increase observed in jobs, income (albeit more slowly) and credit continue, therefore, to foster household consumption.

Variation in commodity prices and in the inflation rate in Brazil

Comparison with the previous month (in %)

Drop in commodity prices quickly affected the Brazilian inflation

Indices for commodities and inflation

	june	july	august
Total	**5,73**	**1,54**	**-10,68**
Food and beverages	4,08	-0,56	-6,66
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Source: IMF, IBGE and FGV

Drop in commodity prices creates conditions for Central Bank to interrupt monetary squeeze cycle

The impact of the decline in commodity prices on inflation indices in Brazil has changed the prospective inflation scenario. However, given the rigidity of service prices and of the core inflation and considering the minutes of the last Copom meeting, the Central Bank is expected to maintain the monetary squeeze while progressively reducing Selic rate hikes. Although there is space for interrupting the contractionist monetary cycle, CNI believes that Copom will increase interest rates by 0.5 percentage points at its October meeting and by 0.25 percentage points at its December meeting – the last one in this contractionist cycle –, meaning that the basic interest rate will close 2008 at 14.5%. As a result of this higher Selic rate, real average interest rates are expected to rise from 6.3% to 6.6% this year.

The current monetary policy was not designed to deal with a crisis such as the one being faced now

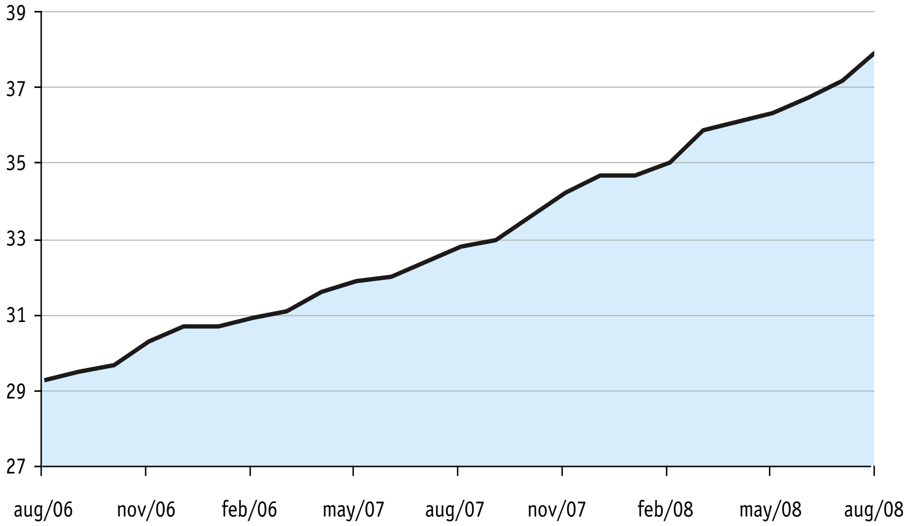
It should be stressed that, in a scenario of higher interest rates, the Central Bank reduced the compulsory deposits of banks twice in less than a week. In the first reduction, the amount to be deducted by financial institutions from the additional requirements imposed on time deposits, savings deposits, and demand deposits was increased from R$ 100 million to R$ 300 million. In the second reduction, the Central Bank changed the requirements imposed on compulsory deposits in federal bonds. In practice, the institution authorized 40% of the compulsory deposit on time deposits to be used by banks to purchase credit portfolios from smaller institutions as an attempt to ease the difficulties faced by these institutions to get credit in the current scenario.

The changes applied to compulsory deposits in a scenario of a rising Selic rate are paradoxical, as they characterize a monetary policy marked by forces acting in opposite directions: at the same time that the Central Bank made credits more expensive by increasing interest rates,

Credit growth as a percentage of the GDP

In %

Credit growth will not keep the same pace



Source: Central Bank of Brazil

it ensured more liquidity to the financial system by reducing the amount of compulsory deposits.

Leasing continues to be the fastest-growing credit modality

Total credit outstanding in the financial system increased by 31.5% in August in relation to the same month in the previous year. This increase made it possible for credit to hit the mark of 38% of GDP, which constitutes an expansion of 5.2 percentage points in relation to the same month in 2007. The result in August constitutes the highest percentage of credit in relation to GDP since the beginning of the Central Bank historical series (1988).

The increase in credit is still mainly determined by credit with non-earmarked resources – which grew by 35.0% in the last 12-month period –, while consigned credit, in the BNDES transfer modality, grew at a less significant rate, 19.9%.

Within credit with non-earmarked resources, leasing continued to be the modality that grew most in the last 12-month period both for natural persons and corporations, particularly in operations for purchasing vehicles. Altogether, leasing increased by 135.3% in August for natural persons and by 75.4% for corporations. As a result, interest rate reference credits for the purchase of vehicles – on which IOF (Tax on Financial Operations) is charged – declined from a growth of 31.4% in August 2007 to a drop of 35.3% in August 2008 (both variations as compared to the same month in the previous year).

Despite the strong growth of credit observed in Brazil, signs of a US crisis contagion can be felt in this sector already. As a result of the strong volatility of the share market and of a lower international financial liquidity, IPOs were interrupted at Bovespa with the aim of breaking the trend of a more intense use of this modality for raising resources. In this scenario, credit has also become scarcer for exporters and for enterprises that rely on international credit lines.

fiscal policy

Fiscal policy reduces anti-inflationary bias

Central Government spending has been growing at a faster pace in recent months

Various pressure sources played a role in increasing public-sector spending in the third quarter of 2008. Although this movement has not led the fiscal policy to resume the expansionist path observed in the past four years, it suggests that its coordination with the monetary policy to control inflation will not be maintained.

Spending with staff, defrayal and investments has pushed Central Government spending up

The primary spending of the Central Government has increased by 5.7% in real terms (IPCA) in the first eight months of 2008 as compared to the same period in 2007. The same comparison made for the first five months of the year revealed a real growth of 4.1%. All the main components of the primary spending contributed to a faster growth pace.

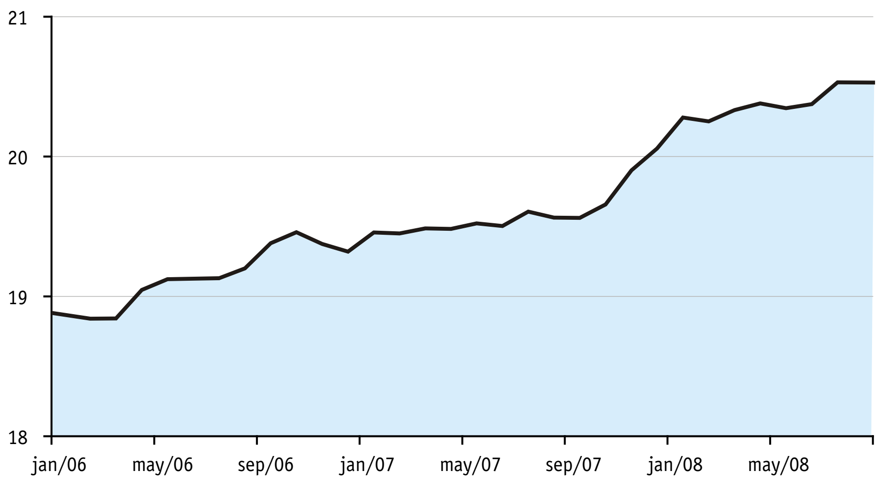
Defrayal and capital spending, which up to May had grown at a real rate of 5.7%, increased in real terms by 8.3% between January and August 2008 in relation to same period in the previous year. Spending with staff, which had grown by 2.1% in real terms in the first five months of the year, had a real increase of 3.7% between January and August 2008 as compared to the same period in the previous year. Finally, social security spending increased from 4.3% up to May to 5.0% up to August.

This spending behavior was counterbalanced by the fact that revenues continued to grow at a spectacular pace. In the first eight months of 2008, the net revenue increased by 10.9% in real terms. This result exceeds the one registered up to May, when the net revenue grew by 10.0% in real terms.

Evolution of the tax revenues of the Central Government

As a percentage of the GDP

Between aug/07 and aug/08, tax revenues in 12 months grew 1.0 percentage point in relation to the GDP.



Source: Central Bank of Brazil   Projection: CNI

Municipal elections and higher tax revenue lead to a higher state and municipal spending

In relation to the spending of state and municipal administrations, despite a slowdown in its growth pace in recent months, the real increase of 16.3% observed in the first seven months of 2008 in relation to the same period in the previous year deserves special mention. This behavior is explained by upcoming municipal elections and higher revenues. In the first seven months of this year, revenues increased by 13.9% in real terms in relation to the same period in 2007. Over the last year as a whole, the tax revenue of states and municipalities had a real growth of 7.2% in relation to 2006. Except for the percentage legally allocated to interest payments provided for in debt renegotiation agreements with the federal government, higher revenues imply greater spending possibilities.

Higher revenues prevent primary result from deteriorating

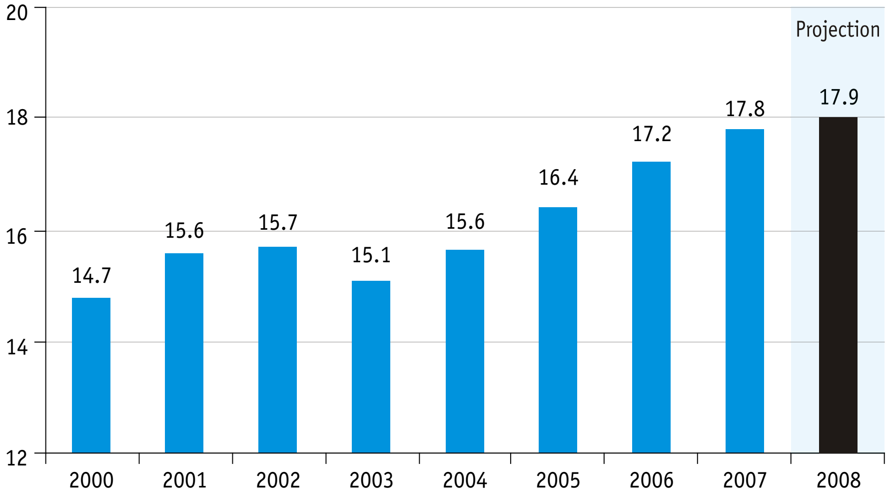
Despite the higher spending registered at the three public management levels, the revenue growth pace was sufficient to prevent the primary result from deteriorating. For the Central Government, the primary surplus accumulated in 12 months increased from 2.78% of GDP in May to 2.99% of GDP in August. For regional governments and their enterprises, the bottom line remained virtually stable, as it increased from 1.09% to 1.10% of GDP. These results led the consolidated public sector primary surplus (Central Government, regional governments and state enterprises) accumulated in 12 months to increase from 4.35% to 4.42% of GDP, despite the lower bottom line of federal state enterprises.

Primary spending of the Federal Government is expected to grow, in real terms, by 6.5% in 2008 in relation to 2007

Evolution of the public sector net debt/GDP ratio

As a percentage of GDP

Primary spending of the central government is expected to show the smaller growth in relation to the GDP in the last five years



Source: Central Bank of Brazil
Projection: CNI

Primary surplus is expected to achieve the target of 4.3% of GDP

The Central Government spending is expected to continue to grow over the next few months. Spending with staff, defrayal and capital is likely to pick up speed until the end of the year. The impacts of the minimum wage on unemployment insurance, salary bonuses and social security benefits will continue to press defrayal and capital spending up. In addition, R$ 5.1 billion in discretionary spending were eliminated in the last budget and financial programming decree. As for spending with staff, apart from the continued effects of salary raises granted early this year, the impacts of wage adjustments granted in the second half of this year will also be felt, which will add R$ 3.5 billion to these expenditures before 2008 is over. Therefore, our projection is that the primary spending of the Federal Government will grow, in real terms, by 6.5% in 2008 in relation to 2007.

On the revenue side, our estimate is that the net revenue will grow by 9.0% in real terms. In this scenario, it is likely that the Central Government will have a primary surplus amounting to 2.8% of GDP and exceed its expanded target (2.7% of GDP).

As for regional governments and their enterprises, the simultaneous slowdown observed in their spending and, mainly, revenue growth pace is likely to enable them to exceed their primary surplus target (0.95% of GDP) again, as in previous years. We expect states and municipalities to close the year with a primary surplus of about 1.05% of GDP.

The bottom line of the Central Government and of regional governments is expected to counterbalance the fact that the primary surplus target (0.65% of GDP) established for federal state enterprises will not be achieved. It should be highlighted that most investments contemplated in the PAC (Growth Acceleration Program) are to be made by these enterprises. In the first six months of 2008, federal state enterprises increased their investments by 8.8% in real terms. Although this behavior is positive for promoting economic growth, it jeopardizes the efforts being made to generate a primary surplus. For this reason, we expect the consolidated public sector to achieve the primary surplus target of 4.3% of GDP.

Broader fiscal indicators have not revealed a truly favorable evolution. We have raised the nominal deficit estimate from 1.7%, as indicated in the last Report, to 1.9% of GDP. This upward review was mainly determined by the faster pace at which the basic interest rate has been rising, beyond what we expected. Despite a higher nominal deficit, the expectation that GDP will grow more is expected to lead to a more pronounced reduction in the debt/GDP ratio. Our estimate is 40.4% of GDP, against the 40.6% projected up to then.

foreign trade sector and the exchange rate

Uncertainties lead to strong exchange rate oscillations

Prospects for 2009 are unfavorable to exports

September was marked by abrupt changes in the exchange parity of the real. In relation to the US dollar, the average exchange rate rose by 11.6% and reverted all the appreciation registered during 2008, which in July hit the mark of 10.9%. However, the devaluation of the real in relation to the US dollar should not be interpreted as a new trend. This is a moment marked by huge uncertainties which are giving rise to strong oscillation in the foreign exchange market.

September was also marked by the worsening of the US crisis. Other countries are facing difficulties already: European banks have been nationalized or sold in the last days of the month. After interventions in several banks, the US Central Bank (FED) and the Treasury of that country announced measures of a more systemic nature to help the financial system. However, the upcoming elections in the US are contaminating and postponing discussions on the package, despite the consensual position that a systemic measure to help the financial system is necessary. The dimension of the crisis and the effectiveness of the measures being proposed are not clear, leading to great insecurity in markets.

September was marked by the worsening of the US crisis

The Central Bank of Brazil, in turn, has been carrying out auctions to put the breaks on speculation on the price of the US dollar in the domestic market after a strong devaluation of the domestic currency in September. This action of the Central Bank revealed its intention to mitigate oscillations in the exchange rate of the US currency.

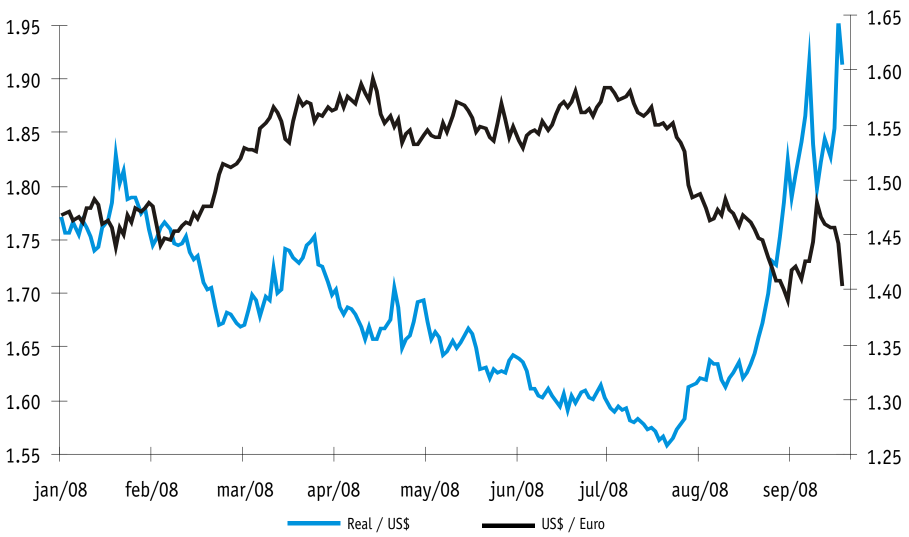
The worsening of the US crisis has been pushing the price of the US dollar up for two reasons. As risk aversion increases, investors prefer to invest in bonds that are considered safer, such US Treasury bills, strengthening the US currency throughout the world. For the real, higher profit remittances are being sent abroad to make up for damages in their head offices. This stimulus has led to a more intense exit of US dollars than initially projected and, consequently, to a more pronounced current account gap deterioration.

Therefore, the Central Bank is expected to take similar measures this quarter to avoid strong oscillations in the price of the US currency. As a result, we are projecting an exchange rate of about R$ 1 / US$ 1.80 at the end of the year.

Nominal exchange rate

Daily values

Dolar appreciates in comparison to Real and Euro



Source: Central Bank of Brazil

Export prices rise to record levels

Brazilian exports increased by 29% in the first nine months of this year in relation to the same period in 2007. It should be stressed, however, that the increase registered in the exported value is exclusively attributed to an increase in export prices. From January to August, prices increased by 29%, while the exported volume dropped by 1% as compared to the same period in 2007. In August, the price indices calculated by Funcex hit record levels, accumulating an increase of 52% in two years.

Despite the drop in commodity prices in the international market, prices are still higher than those prevailing in 2007. In addition, exports had been partly contracted already, meaning that the impact of these changes on prices will only be felt when contracts are amended, which can take a few months. The same reasoning applies to the devaluation of the real, which in principle would favor sales abroad.

Therefore, given the positive results of exports in the second quarter and beginning of the third quarter, total exports are expected to amount to US$ 208 billion in 2008, 30% more than in 2007. It should be mentioned, however, that this growth depends even more on prices than had been anticipated early this year.

Prospects for 2009 are rather negative. There is increasing evidence that other key economies will also be affected by the US crisis. Other countries will be affected by a lower international economic growth, which will have an additional negative effect on Brazilian exports, but only in 2009. In addition, credit will be less available in the international market, affecting export financing.

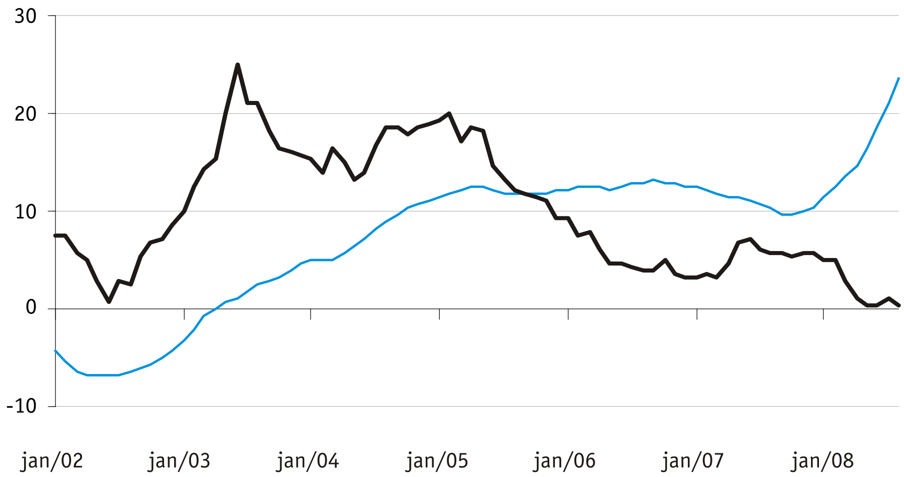
Imported volume has been growing at a steady pace

Imports continue to grow at a fast pace and hit the mark of 52% in the first nine months of 2008 as compared to the same period in 2007. Price gains and the increase observed in the imported volume have been sustaining this growth. Prices increased by 20% in the 12-month period ending in August, while the imported volume grew by 23% in the same period. Prices continue to rise at a fast pace, which is mainly explained by the hike in the prices of petroleum and of its by-products. The imported volume, in turn, continues to grow at a steady rate,

Exports: Price and quantum indices

Variation (%) between the average registered during the past 12 months and the one observed in the previous 12 months

Prices are rising and quantum is stable



Fonte: Funcex Elaboração: CNI

sustained by the economic activity and by domestic demand.

The fact that import prices continue to rise led us once again to review total imports upward in 2008, which in our estimate will amount to US$ 183 billion, a growth of almost 52%. The trade balance, therefore, would amount to US$ 25 billion.

Profit remittances increase current account deficit

The current account accumulated a deficit of US$ 21.9 billion, or 1.45% of GDP, in the twelve-month period ending in August. This deficit resulted from a combination of two factors. On the one hand, the increasing difference between the growth pace of exports and imports reduced the trade balance accumulated during the year. On the other hand, the deficit with services and income is also increasing.

The appreciation of the real in relation to the US dollar led to a higher spending with services and, as a result, the deficit with services increased by 36% in the 12-month period ending in August. Net profit remittances abroad increased by 40% (US$ 2.3 billion) in the same comparison, reflecting the need felt by foreign companies to remit income from enterprises operating in Brazil. Direct foreign investments, in turn, amounted to a net figure of US$ 32.7 billion in 12 months, accumulating a sum equivalent to 2.17% of GDP.

> Deficit in current account of services and income increased by over 1/3

Net profit remittances abroad remained quite high throughout the year and the worsening of the US economic crisis is expected to lead to even higher remittances. Domestic demand is also still on the rise, making it possible to predict that spending with services will continue to grow in 2008. Therefore, we project a current account deficit of US$ 29 billion at the end of the year, about 1.77% of GDP.

CNI

Prospects for the Brazilian economy

	2006	2007	2008 *estimate*	2008 *Earlier projection jun/08*
Economic activity				
GDP (annual change)	3.8%	5.3%	**5.3%**	4.7%
Industrial GDP (annual change)	2.9%	4.9%	**5.5%**	5.0%
Household Consumption (annual change)	4.6%	6.5%	**6.0%**	5.5%
Gross Fixed Capital Formation (annual change)	10.0%	13.4%	**13.5%**	10.5%
Unemployment Rate (annual average- % of EAP)	10.0%	9.3%	**7.9%**	8.04%
Inflation				
Inflation (IPCA - annual change)	3.1%	4.2%	**6.2%**	6.4%
Interest rates				
Nominal Interest Rate				
(average annual rate)	15.40%	12.13%	**12.70%**	12.50%
(end of period)	13.25%	11.25%	**14.50%**	14.25%
Real Interest Rate (average annual rate and IPCA)	10.7%	8.2%	**6.6%**	6.3%
Public accounts				
Nominal Public Deficit (% of GDP)	3.0	2.3	**1.9**	1.7
Primary Public Surplus (% of GDP)	3.9	4.0	**4.3**	4.3
Net Public Debt (% of GDP)	44.9	42.8	**40.4**	40.6
Exchange rate				
Exchenge Rate - R$/US$				
(average annual rate)	2.14	1.78	**1.80**	1.67
(end of period)	2.18	1.95	**1.72**	1.67
Foreign sector				
Exports (Billion US$)	137.5	160.0	**208.0**	190.0
Imports (Billion US$)	91.4	120.0	**183.0**	170.0
Trade balance (Billion US$)	46.1	40.0	**25.0**	20.0
Current Account Balance (Billion US$)	13.6	4.5	**-29.0**	-20.0

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