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Better economic scenario is not sufficient to ensure strong growth

The Brazilian economy is expected to grow by 2.4% in 2013. Although higher than in 2012, this growth rate is still unsatisfactory. Industry GDP is up by 1.4%, representing an improvement from last year's decrease. The composition of growth is another positive point, with investment contributing more significantly to the increase in GDP.

On the other hand, the foreign trade sector (net exports) is still contributing negatively to economic growth. Undoubtedly, the high trade deficit in manufactured goods – which has been at around US$ 100 billion annually for the past three years – is a clear sign of the difficulties faced to improve industry performance and GDP.

The resumption of growth is also limited as inflation remains close to the target ceiling. The current level of interest rates, which will likely continue beyond 2013 to cope with pressures from services and from the effects of the exchange rate devaluation, creates additional barriers to recovery. Maintaining an expansionary fiscal policy does not help much and ultimately imposes disinflation costs on the productive sector.

The low-growth scenario reflects the difficulties to address two structural challenges: low competitiveness and low investment rates (less than 20% of GDP).

There is a consensus that it is essential to increase our competitiveness by reducing production costs and increasing productivity. However, the slow and sometimes incomplete implementation of policies in this area ends up not being enough to reverse the situation.

Changes in the exchange rate level are a relevant factor, even though short-term volatilities make it more difficult for the new level of the Brazilian currency to be perceived. Once this moment is over, the effects of these changes will be more and more noticeable.

Progress in terms of investment has been less impressive. The domestic savings rate is still low, requiring greater borrowing of foreign savings (current account deficit). This alternative could lead to a weakening external scenario, as a result of lower global availability of resources with the anticipated normalization of US monetary policy.

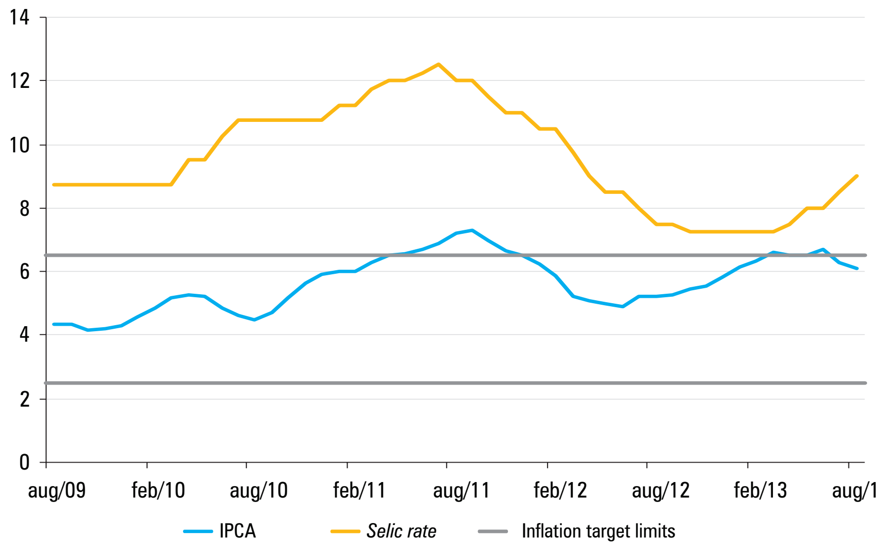
In short, the economic environment has been improving gradually. The challenge lies in enhancing this improvement and making it permanent. Investment is the key issue and the infrastructure agenda provides a great opportunity. Putting this agenda into practice requires long time horizons and high confidence. In this particular regard, the commitment to a clear and credible, yet less ambitious fiscal target helps underpin confidence in economic fundamentals and enhance the public sector's ability to promote savings and investment.

The Brazilian economy in the third quarter of 2013

IPCA and *Selic* rate

12-month figure (IPCA) and percentage per year (*Selic*)

New monetary tightening as inflation remains close to target ceiling



Source: IBGE and Central Bank of Brazil

economic activity

GDP grows as investments rise

More balanced economic growth

The up-and-down trend in activity indicators is the most striking feature of the Brazilian economy evolution in 2013. Nevertheless, CNI revised its estimate for GDP growth in 2013 upward from 2.0% to 2.4%.

GDP grew by 1.5% in the second quarter from the quarter before, more than double the figure for the first quarter on the same comparison basis. With this result, the Brazilian economy would grow by at least 2.2% this year, assuming that GDP will hold steady in the year's third and fourth quarters (dragging effect).

Consumption is replaced by investment in GDP growth

While business confidence has slumped to a record low, investments – as measured by gross fixed capital formation (GFCF/IBGE) – grew by 6.0% in the first half of 2013 from the same period last year.

Transport equipment (mainly for trucks) accounted for most of the growth in production of capital goods in Brazil. The production of these products, however, shows signs of slowdown: the growth rate fell from 28% in June to 16% in July on a year-over-year basis.

Except for agricultural products, the year-on-year growth rate for all categories of capital goods has decelerated. The expansion in the production of capital goods for industrial use dropped from 21.4% in June to 13.3% in July.

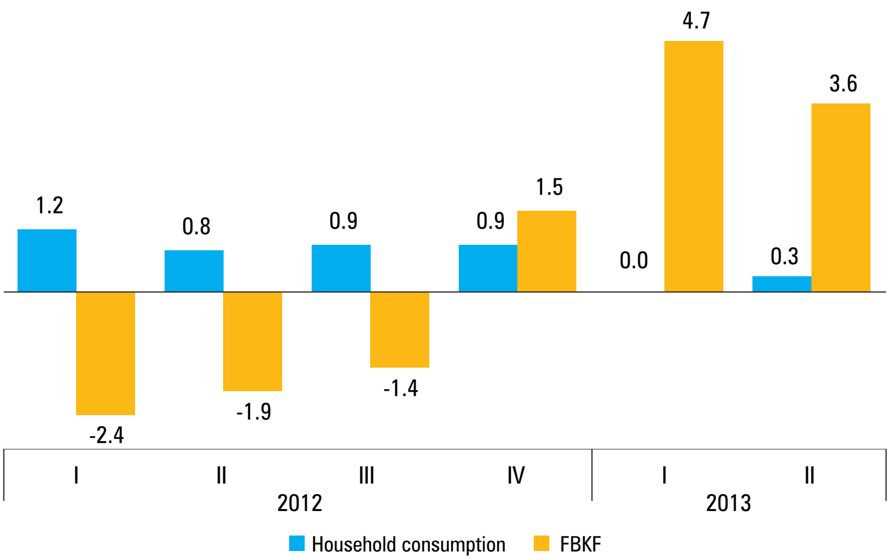
According to the Monthly Survey of Industry - Physical Production (PIM-PF/IBGE), total production of capital goods fell by 3.4% at the beginning of the quarter in July month on month. Despite the lower growth rate and less widespread investments, CNI expects GFCF to grow by 8.0% in 2013, thus contributing 1.5 percentage points to GDP growth.

Household consumption increased by only 2.2% in the first half of 2013 from the same period the year before. The slowdown in employment growth, increasingly smaller gains in workers' real earnings, and high household debts will result in household consumption growing by no more than 2.0% in 2013. Should this be confirmed, household consumption will contribute 1.2 percentage points to GDP growth in the year – less than investments.

Household consumption and investment (GFCF)

Quarter-on-quarter variation - seasonally adjusted (%)

Investment shows clear signs of recovery and growth in household consumption slows down



Source: IBGE

Manufacturing activity down at beginning of third quarter

Industrial production fell by 2.0% in July from a month earlier. The drop in July was double the entire growth observed

in the second quarter. The Central Bank's Economic Activity Index (IBC-BR), which is used as a proxy to observe the monthly evolution of GDP, declined by 0.3% in July month on month.
Industrial stocks remain above planned levels. In August, the indicator for actual-planned stock levels (CNI Industrial Survey - Manufacturing and Mining) stood at 51.3 points. To bring stock levels back down to planned levels, industry will have to reduce its production growth rate.

While some indicators show a decline in activity early in the third quarter, others point to better results. The Business Confidence Index (ICEI/CNI) rose in August and September. The ICEI is up for the second consecutive month after remaining close to the dividing line between confidence and lack of confidence, which is an important sign of industry recovery.

Considering the statistical dragging effect of 2.1% of manufacturing GDP and the drop in industrial production in July, CNI expects to see a 2.6% growth in manufacturing GDP in 2013, positioning manufacturing as the highest-growing industrial sector in the year. Mining and quarrying GDP is expected to decline by 4.0%, contributing negatively to the sector's GDP.
Taking all four industrial segments together, the sector's GDP is projected to grow at a rate of 1.4% in 2013.

Retail sales are up by 1.9% in July month on month as a result of an accelerated growth rate in observed in recent months. The services GDP rose by 1.8% in the year's first half as compared to the same period one year ago. Considering the trade results at the beginning of the quarter, CNI is expecting services GDP to rise by 2.2% in 2013.

On the demand side, the devaluation of the Brazilian currency (real) will likely have a more significant impact on exports only next year, with foreign sales remaining virtually unchanged in 2013 year on year. Imports in turn are expected to keep growing in the year (6.0%). As a result, the foreign trade sector will contribute negatively to GDP by 0.8 percentage points in 2013.

Economy holding steady in third quarter

Notwithstanding an apparent improvement in the composition and pace of economic growth, activity indicators continue to show month-to-month ups and downs, a clear sign of low economic growth.

After the disclosure of the few activity indicators for the July to September period – industrial production, IBC-BR, business confidence, and retail sales – there is no evidence that the same growth rate observed during the second quarter will linger on.

CNI estimates that the economy will hold steady in the third quarter (-0.3%) and grow again in the last quarter of 2013 at a similar pace as in the first quarter, resulting in GDP growing by 2.4% in 2013.

CNI's GDP estimate
Percentage variation and components' contribution to GDP

	GDP components	2013 Growth rate (%)	2013 Contribution (p.p.)
Demand side	Household consumption	1.9	1.2
	Government consumption	1.5	0.3
	Gross formation of fixed capital	8.0	1.5
	Exports	0.0	0.0
	(-) imports	6.0	-0.8
Supply side	Agriculture/livestock	11.0	0.6
	Industry	1.4	0.4
	Mining and quarrying	-4.0	-0.2
	Manufacturing	2.6	0.3
	Construction	2.0	0.1
	Public administration, health and public education	2.2	0.1
	Services	2.2	1.5
	GDP	**2.4**	

employment and income

No room for further declines in unemployment rate

Employment and labor force growing at same pace

The pace of job creation reached its lowest point in May 2013, when year-on-year employment increased by a mere 0.1%, meaning that only 23,000 jobs were created in 12 months in the six largest Brazilian metropolitan areas (Monthly Employment Survey - PME/IBGE).

The downward trend in the labor market, however, has recently come to a halt. In June and July, metropolitan employment started to grow more strongly and posted a year-on-year increase of 1.5% last month. This growth represents 339,000 new jobs created in the last twelve-month period.

Labor market formalization keeps growing

Even in a sluggish labor market, formal employment continues to grow more than informal jobs. Formal jobs have grown year on year for 45 consecutive months. In the private sector, formal employment expanded at a rate of 3.5% in July from the same month last year. Thus, the pace of formal employment growth has remained above that of economic growth, characterizing an inclusive labor market.

Informal jobs continue to drop steadily on the same comparison basis. In July, they fell by 5.6% also on a year-on-year basis. Self-employment has begun to grow again, but still less than formal jobs.

As a result, the labor market formalization index remains on an almost uninterrupted upward trend. In July, this indicator, which is calculated by the sum of all formal and statutory jobs divided by all occupations, amounted to 62.7%, a record high since the series started in March 2002.

However, the pace of employment growth has been declining and is yet to show signs of reversing this trend. Data from the General Registry of Employed and Unemployed Persons (Caged/MTE) indicate a slowdown in the job creation pace in Brazil. After hitting 2.3 million jobs in the 12 months ending August 2010, the downturn in employment growth continued until the number of new jobs reached 388,000 in July 2013, also on a year-over-year basis.

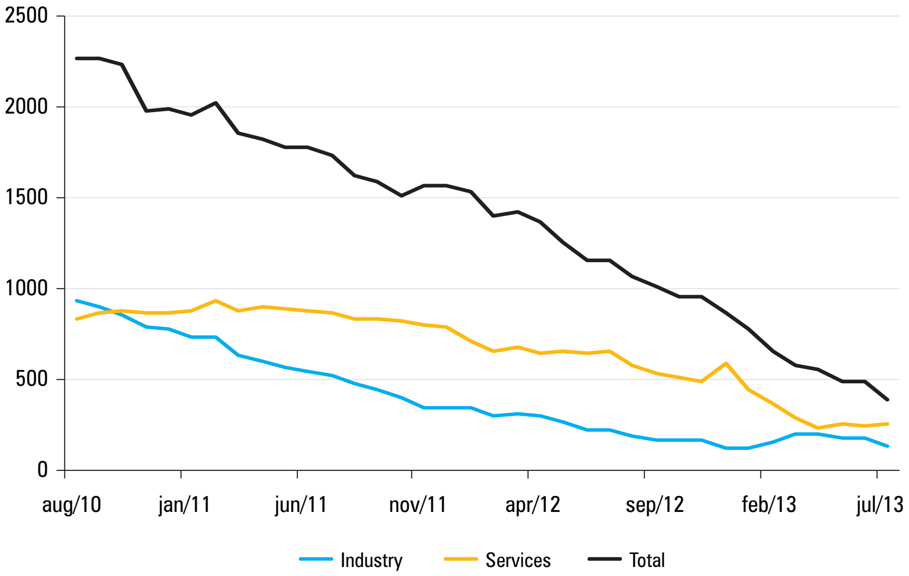
Job creation in services and industry (comprising the four segments) also lost steam. In August 2010, nearly 900,000 jobs were created in each sector year on year.

It is worth mentioning that, even in a scenario of significant ups and

Job creation

Year-on-year (in thousands)

All economic sectors experience slowdown in employment growth



Source: CAGED / MTE

downs in industrial activity, there are no signs whatsoever that industry will lay off workers. The strategy of retaining skilled labor is widespread in Brazilian industry. In July, employment in manufacturing (Industrial Indicators/ CNI) grew by 0.3% over the previous month and accumulated a 0.9% increase from the same period in the previous year.

Unemployment rate holding steady in 2013

The proportion of economically active population (EAP) grew steadily from the beginning of 2011 until August 2012. After this period, there was an increased job search activity (EAP grew more significantly), which led the labor force to grow by 1.5% in July 2013 from the same month one year ago.

As a result, the labor force began to grow at a similar pace as employment. If the labor force continues on this trend – the scenario used by CNI – there will be no room for further declines in the unemployment rate. While it will experience a drop in the second half on account of seasonal factors, the average unemployment rate for the year will likely be very close to the 2012 level.

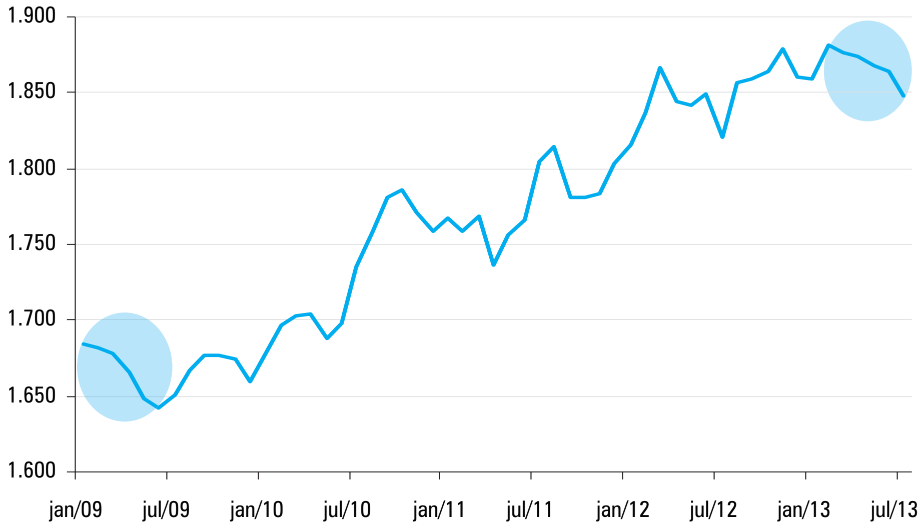
Average real earnings not growing as before

Average real earnings usually earned by workers (PME/IBGE) have been growing almost continuously year on year since 2010. However, this indicator is changing its behavior. As a result of higher inflation, wage negotiations have not been as successful as before. An analysis by Dieese shows that nearly 85%

Average real earnings for metropolitan workers

In R$ - July 2013 prices

Five-month straight decline in average real earnings took place on more than two occasions (early 2003 and early 2009)



Source: PME / IBGE

of the collective bargaining units analyzed in the first half of 2013 managed to secure an increase in real wages in relation to the National Consumer Price Index (INPC/IBGE). This percentage is lower than that observed in 2010 and 2012 and is practically the same as in 2011.

The slowdown in the evolution of workers' real income is evident. This indicator posted the fifth successive month-on-month decline in July. Since the series of the Monthly Employment Survey began in March 2002, a drop of that magnitude was only seen on two other occasions. The first was in 2003, a period of political and economic turmoil owing to the change of government, when GDP grew by only 1.1%. The second occasion was shortly after the international crisis hit Brazil (almost the entire first half of 2009).

Lower earnings growth hinders consumption

While, on the one hand, consumption is not expected to drop, on the other hand, average real earnings have also not shown any signs of more substantial growth.

This behavior points to a more modest evolution of consumption, since the labor market has lost traction and household debt remains high for historical standards.

inflation, interest rates, and credit

Monetary tightening to continue in coming months

Regulated prices hold IPCA within the upper target limit

Brazilian inflation remained on a high level in the third quarter. In August, the 12-month figure for the National Consumer Price Index (IPCA) amounted to 6.09%. Despite the decline (down from 6.70% per year in June), this downward trend is expected to lose steam by year end.

When considering the four major IPCA groups (regulated prices, food, industrial products, and services), one can see that all groups are not actually trending downward.

Food and service prices are still the main responsible for sustaining the IPCA at a high level. Food products are up by more than 10% in the twelve months to August. However, this can also explain the slowdown in the IPCA, since the current level is lower than that in previous months (14% in the 12 months to April).

The slight decrease in the twelve-month figure for the group results from a reversal in the price shock in late 2012 and early this year on account of harvest problems. This downward trend will likely come to a halt by the end of 2013 due to increased pressure on prices caused by a further depreciation in the exchange rate as compared to the beginning of the year. Thus, the group's 12-month figure is projected to close the year slightly below 10%.

In the opposite direction, industrial product prices experienced an unusual increase. The 12-month figure for the group has been above 4.6% since June, the highest level since 2008. The increase in the group's twelve-month figure, which was less than 2% in late 2012, resulted mainly from the reinstatement of the Tax on Industrialized Products (IPI) on cars. This tax was reinstated in January and February this year, while the drop caused by this measure took place in June last year (thus not included in the 12-month figure).

This scenario is not expected to change significantly in coming months, as the exchange rate has a direct impact on the evolution of industrial product prices. The exchange rate devaluation observed through much of the quarter tends to result in these prices increasing more than the monthly seasonal behavior, causing the 12-month figure for the group to remain close to 4.6% in the year.

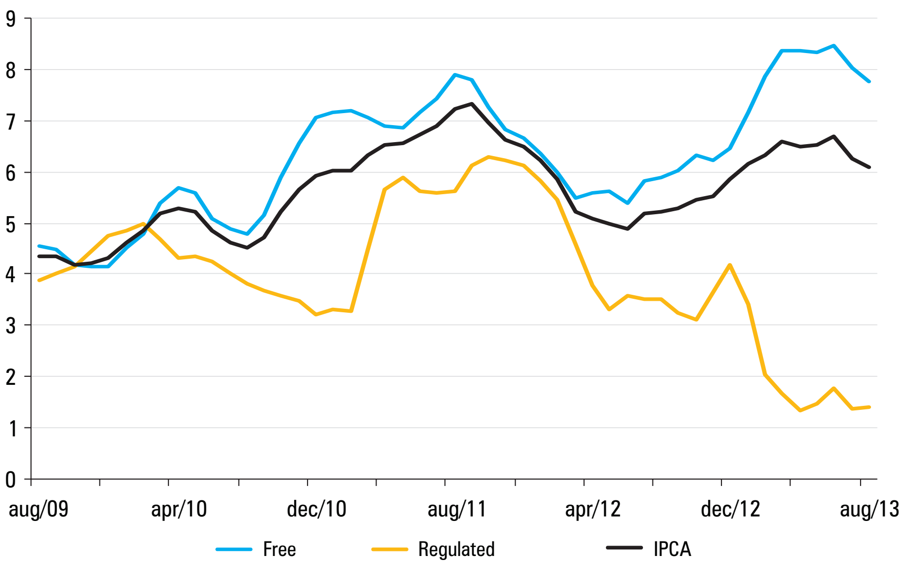
The service group continues to show the same inertia that has characterized the evolution of its prices: the group's 12-month figure reached 8.6% in August. The slowdown that was expected across 2013 is yet to be seen: the figure is at the same level as in late 2012. This level is likely to continue until the end of the year.

The group of regulated prices has experienced an unusual downturn. The group's 12-month figure stood at 1.4% in August, significantly down from the level observed at the end of last year (4.2%), mainly as a result of a reduction in electricity costs and the "freezing" of public transportation fares. As a comparison, if prices were not considered in the IPCA, inflation would total 7.8% in August.

IPCA broken down by market and regulated prices

12-month figure (%)

Regulated prices moving further away from free prices



Source: IBGE – Prepared by: CNI

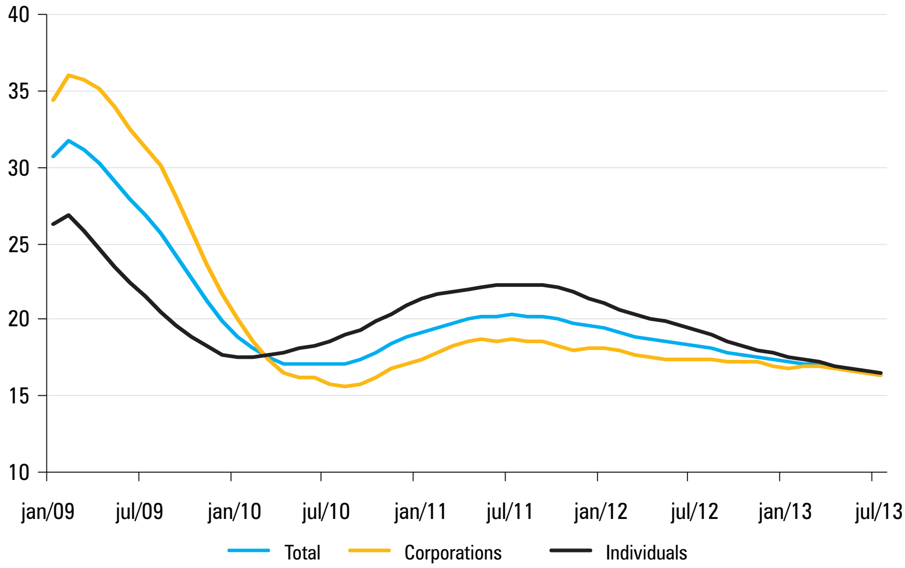
CNI's analysis of the estimates for this group in coming months takes two basic factors into account: (i) electricity price adjustments already approved in some states and the Federal District and (ii) no adjustment in fuel prices. The latter is because it is impossible to make a prediction, as it involves not only political but also technical issues. Despite increases in electricity prices, the 12-month figure for the group will slow down even further, closing the year at about 1%.

Under this scenario, CNI estimates that the IPCA will end the year at 5.8%. Should there be an increase in fuel prices this year (e.g. of 5%), the IPCA would amount to 6.0% in 2013.

Balance of loans

12-month figure as compared to the previous 12 months (%)

Total credit slows down in the year



Source: Central Bank of Brazil

Upward trend in Selic rate to continue at next COPOM meetings

With inflation close to the upper target limit, the Monetary Policy Committee (COPOM) reinstated a monetary tightening policy in April by increasing the Brazilian basic interest rate (Selic). In spite of the low-growth scenario, this policy was maintained in the third quarter on account of difficulties faced to reduce inflation. In 2013 alone, the Selic rate was increased four consecutive times, up from 7.25% per year in April to 9.00% per year in August.

This rising trend is expected to continue in coming months. Inflation will remain at about 6% per year and other factors contribute to a scenario of need of attention to inflation (e.g. exchange rate devaluation and potential fuel price increase).

CNI is therefore expecting to see two new increases by year end, with Selic growing to 9.75% in November and accumulating a monetary reduction of 2.50 p.p. in 2013. In this scenario and with inflation at 5.8%, the average real interest rate will amount to 1.9% per year in 2013, below last year's figure (3.1%).

Interest rates on loans on the rise

Lending has been slowing down in 2013. The balance of total credit in the economy amounted to 16.5% in the year to July, above the figure for the previous twelve-month period. However, this same indicator exceeded 20% in mid-2011.

It is worth stressing that this slowdown is not unique to loans to individuals or corporations, as both are also up by about 16% and losing momentum. The economic slowdown and high household debts contribute to reducing demand for credit. With the possibility of the international scenario returning to normal as a result of a reversal of capital flows to the US, financial institutions are more cautious about granting loans.

Another factor contributing to lower credit growth is the hike in interest rates. The upward trend in the Selic rate is already being reflected in the rates offered by banks: in July, the average interest rate on loans to individuals reached 25.1% per year, against 24.0% per year in May. For corporations, the figure rose from 13.5% per year to 14.4% per year during the same period.

As the upward trend in Selic will likely continue until the end of the year, we can still expect to see new increases in interest rates on loans and financing.

fiscal policy

Primary surplus still far from target

Spending by regional governments strongly on the rise

The growth rate of Federal Government expenditures has not changed in recent months. They had risen by 6.0% in real terms in the January-April period, and posted the same growth when comparing the period between January and July 2013 to the same months in 2012. The increase in federal government spending characterizes the maintenance of an expansionary fiscal policy, particularly when comparing the GDP growth of 2.6% in the first half of 2013 to the same period of 2012.

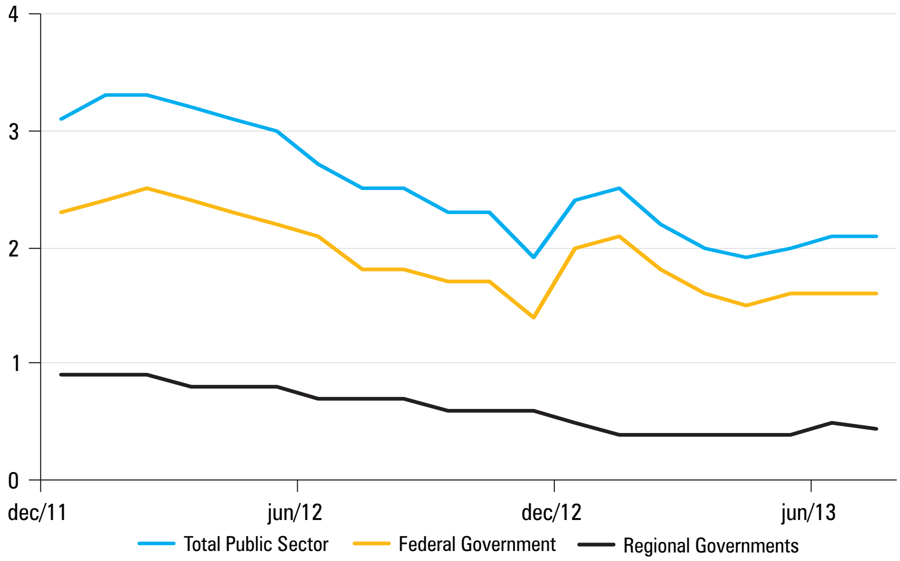
Special mention should be made of the rise in discretionary spending: up by 10.0% in real terms in the first seven months of the year, indicating that fiscal policy has been used as an instrument to boost economic activity. However, defrayal expenditures accounted for most of this growth. Within the item ‘other defrayal and capital expenses’, defrayal spending grew by 13.2% from January to July 2013. On the other hand, investments (GND 4 of the Integrated Financial Management System - SIAFI) posted drop of 2.7% on the same comparison basis.

Spending by states and municipalities in turn experienced a sharp acceleration in its growth rate. Total expenditures, which rose by 2.3% in real terms between January and May 2013, recorded real growth of 7.8% in the first seven months of the year.

Primary surplus of the consolidated public sector and by government levels

In relation to GDP in the last 12 months (%)

Public sector’s primary surplus down by more than 0.3 percentage points of GDP between Dec. 2012 and Jul. 2013



Source: Central Bank of Brazil - Prepared by: CNI

On the tax collection side, the Federal Government’s net revenue experienced real growth of 2.1% between January and July 2013 from the same period the year before. This result represents an increase from the real growth of 0.8% observed in the first five months of 2013. This increase can be explained by the rise in industrial activity and sale of goods and services in June, leading to an increased collection of taxes and charges in July.

On the other hand, the real growth rate of revenues of states and municipalities has experienced a strong decline in recent months. Tax collection, which had increased by 0.6% by April, is now down by 4.6% when comparing the first seven months of 2013 to the same period a year earlier. This fall was driven by a slowdown in transfers to the Federal Government and by a slight drop in the ICMS and other revenue sources.

The evolution of revenues and expenses in the Federal Government over the first seven months of 2013 caused the 12-month figure for the structural primary balance – which excludes atypical factors such as the Brazilian Sovereign Fund – to drop from 1.5% in December 2012 to 1.2% of GDP in July 2013.

For states and municipalities, the significant drop in the rate of revenue growth, coupled with a strong rise in expenses, resulted in a surplus of 0.45% of GDP, far from the target of 0.95% of

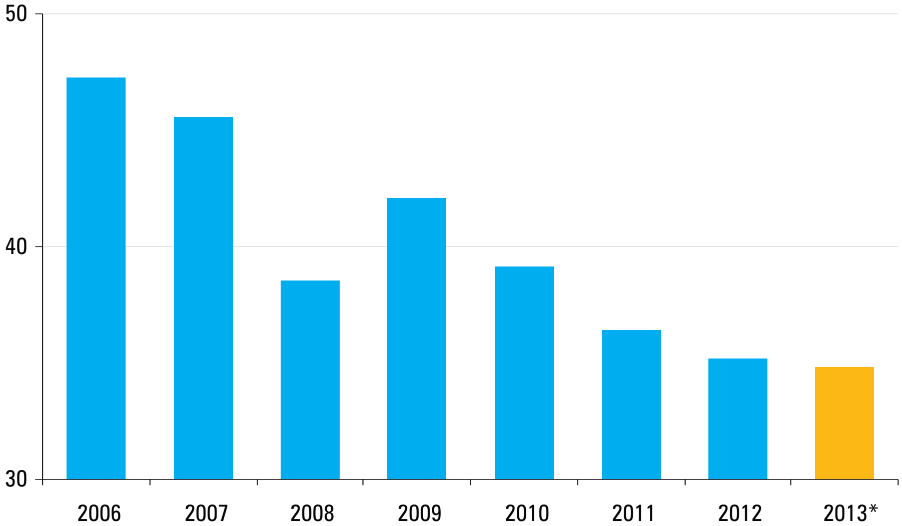
GDP set by the Federal Government. As a result, the primary surplus for the consolidated public sector fell from 2.0% of GDP in December 2012 to 1.6% of GDP in July 2013.

The reduction in the primary surplus led the 12-month nominal deficit to increase from 2.8% in December 2012 to 3.3% of GDP in July 2013. However, the increased nominal deficit has not translated into an increased net debt-to-GDP ratio on account of the exchange rate depreciation. Adjustments in domestic and foreign debts caused the net debt-to-GDP ratio to fall from 35.2% in December 2012 to 34.1% in July 2013. The gross debt-to-GDP ratio in turn continues to grow and reached 59.4% in July, down from 58.7% in December 2012.

Evolution of Public Sector Net Debt

In relation to GDP (%)

Public debt-to-GDP ratio to fall for the fourth straight year in 2013



Source: Central Bank of Brazil
* CNI's forecast

Primary surplus target still distant with timid financing programming

Fiscal policy will likely remain expansionary in coming months. If a new financial programming is not announced, the real growth rate of Federal Government's expenditures is set to accelerate to 7.3% in 2013.

With respect to revenues, CNI is expecting them to grow at a higher rate than that observed until July. Despite the lower growth rate of tax collection in some areas due to tax cuts, the projected increase in revenues not administered by the Internal Revenue Service will likely increase the Federal Government's net revenue to 4.9% in real terms in 2013. In this scenario, the primary surplus for the Federal Government and its state-owned enterprises would hit the mark of R$ 63.7 billion (1.3% of GDP) in 2013.

For states and municipalities, the behavior of expenditures and revenues indicates once again that the requirements under the Fiscal Responsibility Law have not been met. The primary result for regional governments is set to grow less than it did in the January-July period, reaching only R$ 16.9 billion (0.4% of GDP) by the end of the year, well below the level set by the Federal Government (R$ 47.8 billion).

With the aim of achieving the fiscal target, the Federal Government announced an additional financial programming of R$ 4.4 billion in discretionary spending. This new restriction on expenditures authorized in the budget is insufficient and will make it impossible for the primary surplus target to be achieved, even considering the R$ 45-billion rebate authorized by the 2013 Budget Guidelines Law.

Under this scenario, CNI estimates that the consolidated public sector primary surplus will amount to R$ 82.8 billion (1.7% of GDP), falling far short of the adjusted target – considering the rebates – of R$ 110.9 billion or 2.3% of GDP.

The expected result for the primary surplus represents a sharp drop from 2011 (3.1% of GDP) and 2012 (2.4% of GDP). This decline, coupled with an expected slight increase in interest expenses –from 4.9% in 2012 to 5.0% of GDP in 2013 – is expected to cause the nominal deficit to grow to 3.3% of GDP.

The increase in the nominal deficit is unlikely to push the debt-to-GDP ratio up due to the impact of the devaluation in the Brazilian currency on exchange rate adjustments in domestic and foreign debts. Therefore, CNI expects the net debt-to-GDP ratio to drop from 35.2% in December 2012 to 34.8% in December 2013.

foreign trade sector and exchange rate

Close-to-zero trade balance in 2013

Greater need for external financing

Brazilian currency reverses depreciating trend at the end of quarter

The real-dollar exchange rate experienced two different trends in the third quarter of 2013: one began in May and ended on August 22 and the other started on that day. From May 14 to August 22, the Brazilian currency depreciated by 18% against the dollar. From this date until September 20, i.e. in less than a month, the real appreciated again by 9.8%.

Possible changes in the US monetary policy are largely responsible for the recent trend in the exchange rate. Early in the second half, it was taken for granted that the monetary stimulus to the US economy would be withdrawn starting in September. This led to a valuation not only in the Brazilian currency but also in several other currencies, especially in emerging countries.
The fact that the US Central Bank (Fed) had not yet defined its monetary policy also generated significant uncertainty and fluctuations in the values of these currencies during that period. In Brazil, the rapid increase in the external deficit and growing uncertainties among economic agents about economic growth led the Brazilian currency to appreciate more strongly than in other countries.

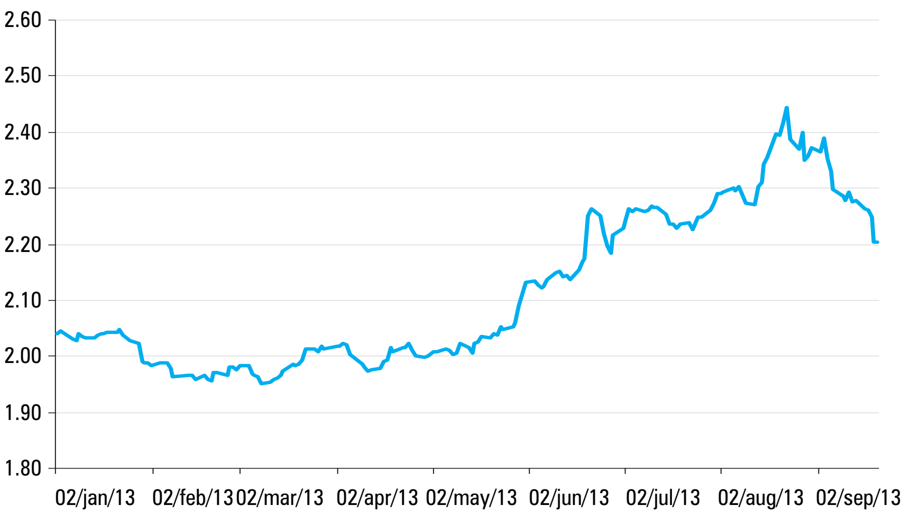
On August 22, however, after the real-dollar exchange rate hit its highest level since 2008 (R$ 2.44/US$), the Central Bank of Brazil (BC) announced that it would hold daily dollar auctions to inject up to US$ 60 billion by year end. Until then, the Central Bank had carried out a series of interventions with little success.

Furthermore, the absence of clear signs of economic recovery in the US reduced the expectation then that the monetary stimulus would be eliminated in September. With this new scenario (on September 18, the Fed decided to await "more evidence" of US economic growth before stopping its stimulus program), the Brazilian currency valuated in a more pronounced fashion.

While the Brazilian currency will likely continue to appreciate temporarily as the market adjusts its expectations about the US market, it will not return to the levels seen at the beginning of the year and is set to devaluate. We forecast an exchange rate of R$ 2.23 /US$ for December and an average of R$2.14/US$ for 2013.

Nevertheless, if the Central Bank decides to reduce or suspend the daily dollar auctions started in August, the Brazilian currency will be more volatile and may depreciate even further.

Real-Dollar Exchange Rate
Ptax Closing Rate (R$/US$)
Brazilian currency reverses depreciating trend seen in the second quarter



Source: Central Bank of Brazil

Exports to drop from 2012 levels

In August, the 12-month figure for Brazilian exports totaled US$ 238.6 billion, down by 4.5% from the twelve months ending August 2012. After a long downward trend started in April

2012, the 12-month export value has held relatively steady and remained slightly below US$ 240 billion since March this year.

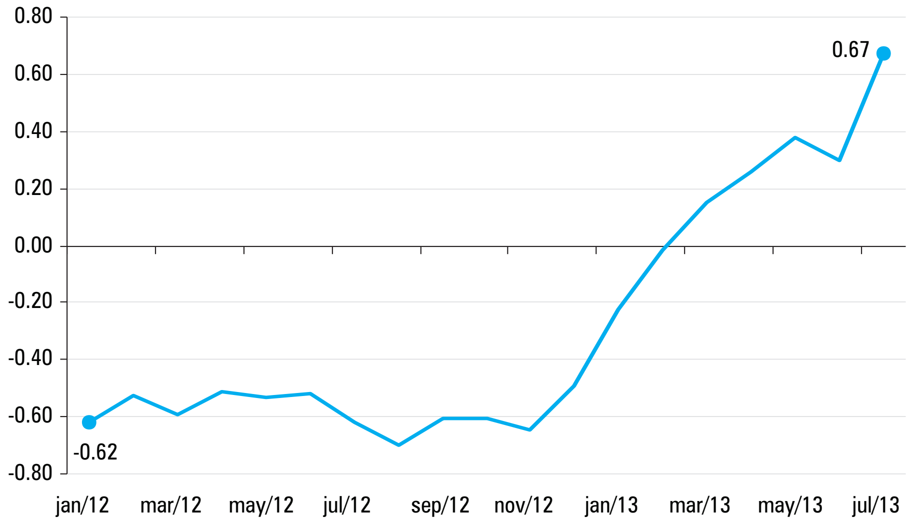
Imports, on the other hand, have trended upward since the beginning of 2013. They totaled US$ 236.1 billion in the 12 months to August, up by 4% on a year-on-year basis. In the same period, the trade balance fell from US$ 22.9 billion to US$ 2.5 billion, down by 89%. Considering that Brazilian exports remained sluggish despite the exchange rate devaluation in the second quarter, the resumption – albeit temporary – of a valuation trend will not improve the short-term scenario. Even if a reversal takes place and the real-dollar exchange rate exceeds the mark of R$ 2.30/US$ or even R$ 2.35/US$ once again, exchange rate fluctuations generate considerable uncertainty, making it difficult for exports to be priced and for investment levels required to boost exports to be defined. Moreover, we will not see a reversal in competitiveness problems and in the adverse external scenario in the short term. Therefore, exports will not show signs of recovery and are expected to remain below last year's level, totaling US$ 240.5 billion in December 2013.

Imports remain on the rise as a result of the new exchange rate level, which is higher than in previous years. Imports will reach US$ 238.8 billion at the end of 2013, up by 7.0% from 2012. As a result, the trade balance will stand at only US$ 1.7 billion in 2013, against US$ 19.4 billion in 2012.

External financing needed

In relation to GDP in the previous 12 months (%)

Need for external financing keeps growing



Source: Central Bank of Brazil

Higher current account deficit as percentage of GDP

In the 12 months to July 2013, the current account deficit reached US$ 77.7 billion, up by 49.8% from the twelve-month period ending in July 2012 (deficit of US$ 51.9 billion). During the period, the foreign trade deficit rose from 2.18% of GDP to 3.39% of GDP.

The decline in the trade surplus over the same period, down from US$ 25.8 billion to US$ 4.5 billion, was responsible for most of the increase in the deficit (74%). The deficit in services and incomes increased from US$ 78.4 billion to US$ 85.1 billion and accounted for the remaining 26% growth in the current account deficit.

Foreign direct investment (FDI) fell by 6% during the same period. FDI amounted to US$ 62.3 billion at the end of July 2013, down from US$ 66.3 billion in the 12 months to July 2012. External financing needed (EFN), i.e. the difference between the current account balance and foreign direct investments, which had been negative until February this year, became positive and has since grown rapidly. In January 2013, EFN was negative at 0.22% of GDP, while in July 2013 it amounted to 0.67% of GDP.

The current account deficit is expected to keep growing until the end of the year. The services account has not responded much to the appreciation of the Brazilian currency in the first half, and the recent reversal of the exchange rate trend could boost spending, especially on international travel. The trade balance will not do much to slow down the pace of deterioration, with the 12-month balance remaining virtually the same until the end of the year. The current account in deficit is therefore expected to hit a record high 2013: US$ 79.6 billion (3.57% of GDP), up by 45.2% from the previous year.

prospects for the Brazilian economy

	2011	2012	2013 *previous projection june/13*	2013 *projection*
Economic activity				
GDP (annual variation)	2.7%	0.9%	2.0%	**2.4%**
industrial GDP (annual variation)	1.6%	-0.8%	1.0%	**1.4%**
Household consumption (annual variation)	4.1%	3.1%	2.3%	**1.9%**
Gross fixed capital formation (annual variation)	4.7%	-4.0%	5.1%	**8.0%**
unemployment Rate (annual average - % of the labor force)	6.0%	5.5%	5.3%	**5.1%**
Inflation				
Inflation (IPCA - annual variation)	6.5%	5.8%	6.0%	**5.8%**
Interest rates				
Nominal interest rates				
(average rate in the year)	11.76%	8.63%	8.25%	**8.27%**
(year end)	11.00%	7.25%	9.50%	**9.75%**
Real interest rate (annual average and deflated rate: IPCA)	4.8%	3.1%	1.7%	**1.9%**
Public accounts				
Nominal public deficit (% of GDP)	2.61%	2.47%	3.40%	**3.30%**
Public primary surplus (% of GDP)	3.11%	2.38%	1.50%	**1.70%**
Net public debt (% of GDP)	36.4%	35.2%	34.9%	**34.8%**
Exchange rate				
Nominal exchange rate - R$/US$				
(average in December)	1.83	2.08	2.18	**2.23**
(average in the year)	1.67	1.95	2.10	**2.14**
Foreign trade sector				
Exports (US$ billion)	256.0	242.6	249.3	**240.5**
imports (US$ billion)	226.2	223.2	240.1	**238.8**
Trade balance (US$ billion)	29.8	19.4	9.2	**1.7**
Current account balance (US$ billion)	-52.5	-54.2	-74.3	**-79.6**

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