



**BANCO CENTRAL  
DO BRASIL**

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

**Mendoza – Argentina – November 2009**

**The Brazilian Reaction to the Financial Crisis**

**Fabio Araujo**

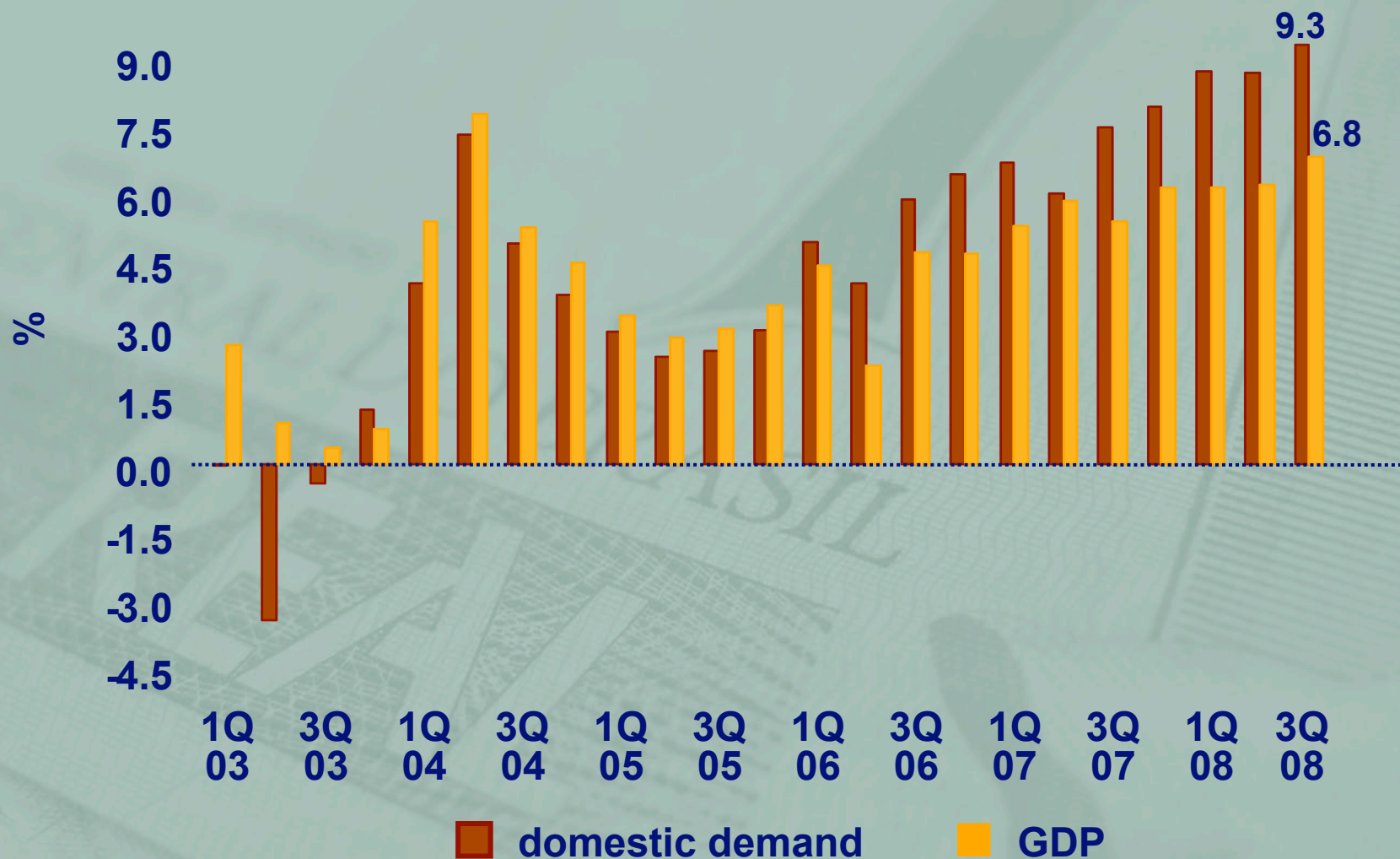
# Outline

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

# Brazil at the Outset of the Crisis

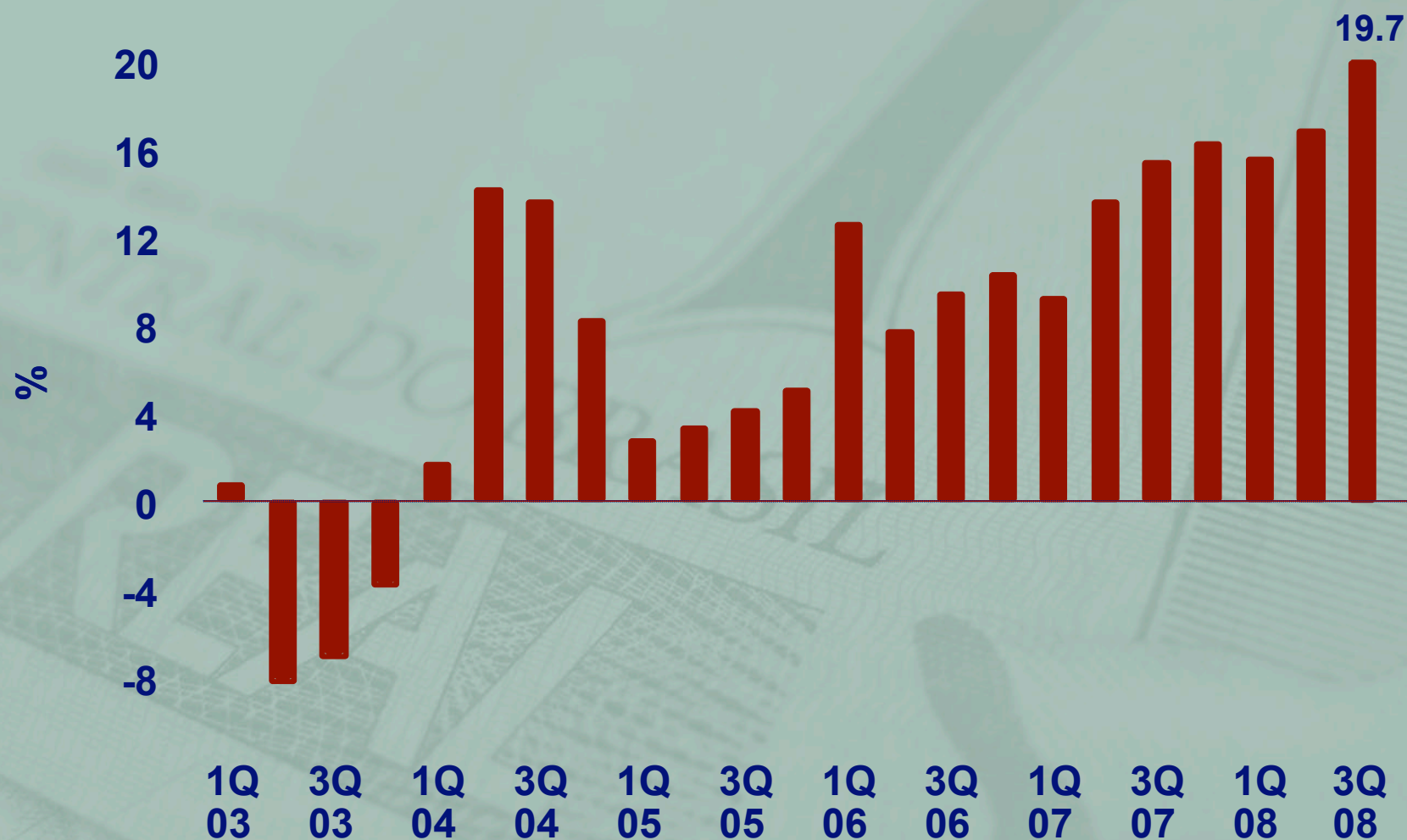
# Domestic Demand and Supply

change year-over-year



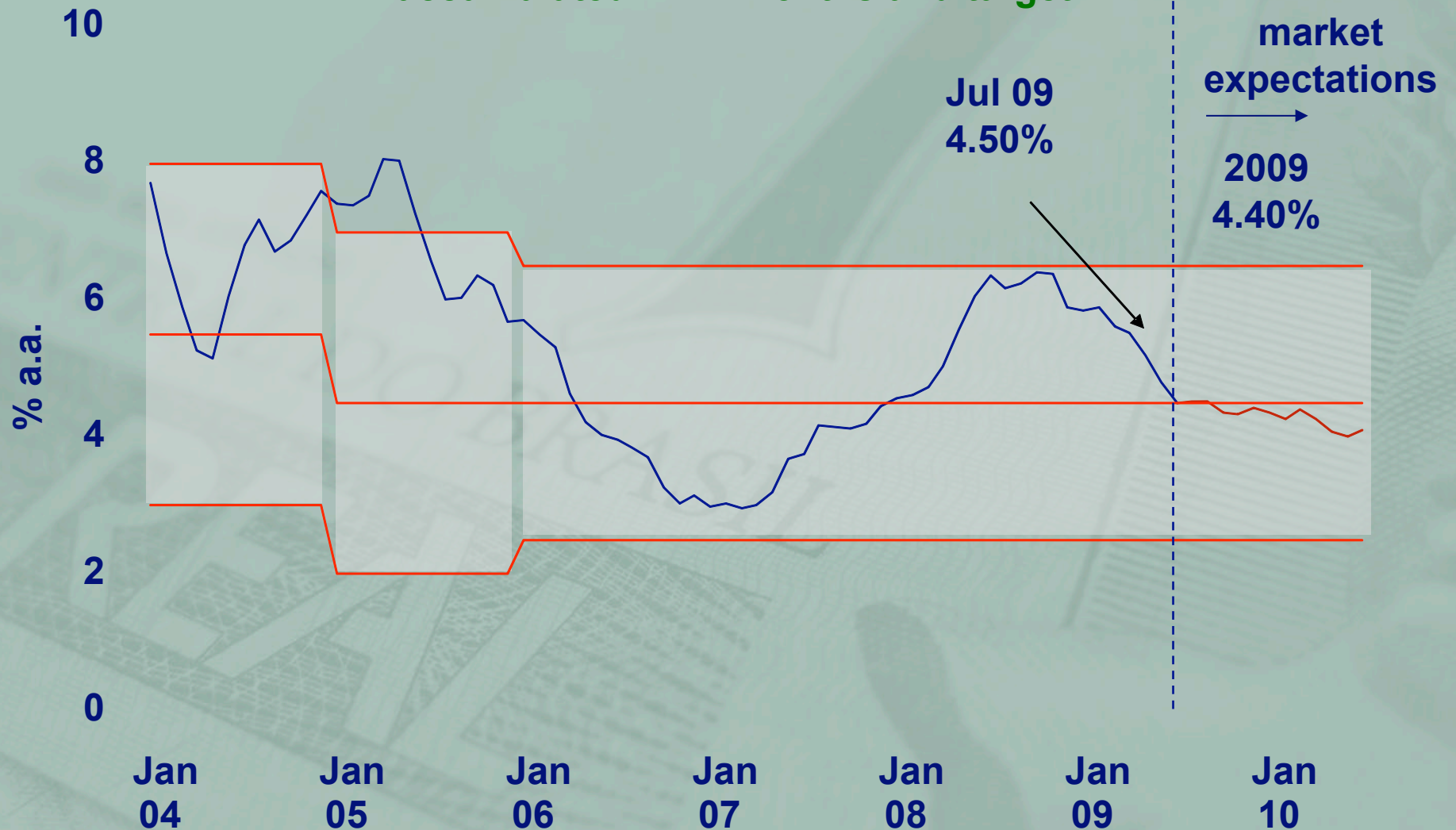
# Fixed-Capital Investment

change year-over-year



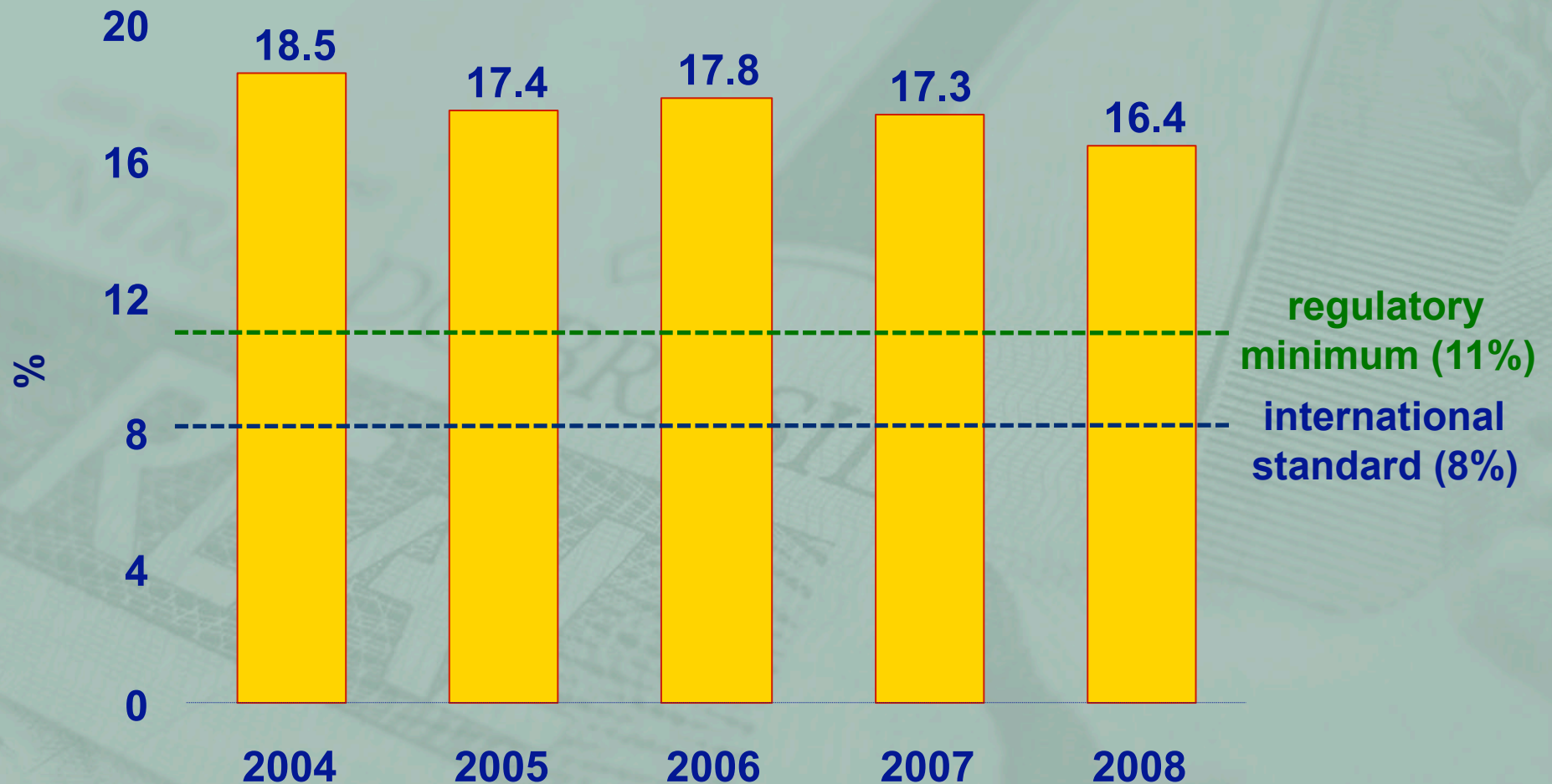
# Inflation

IPCA accumulated in 12 months and target

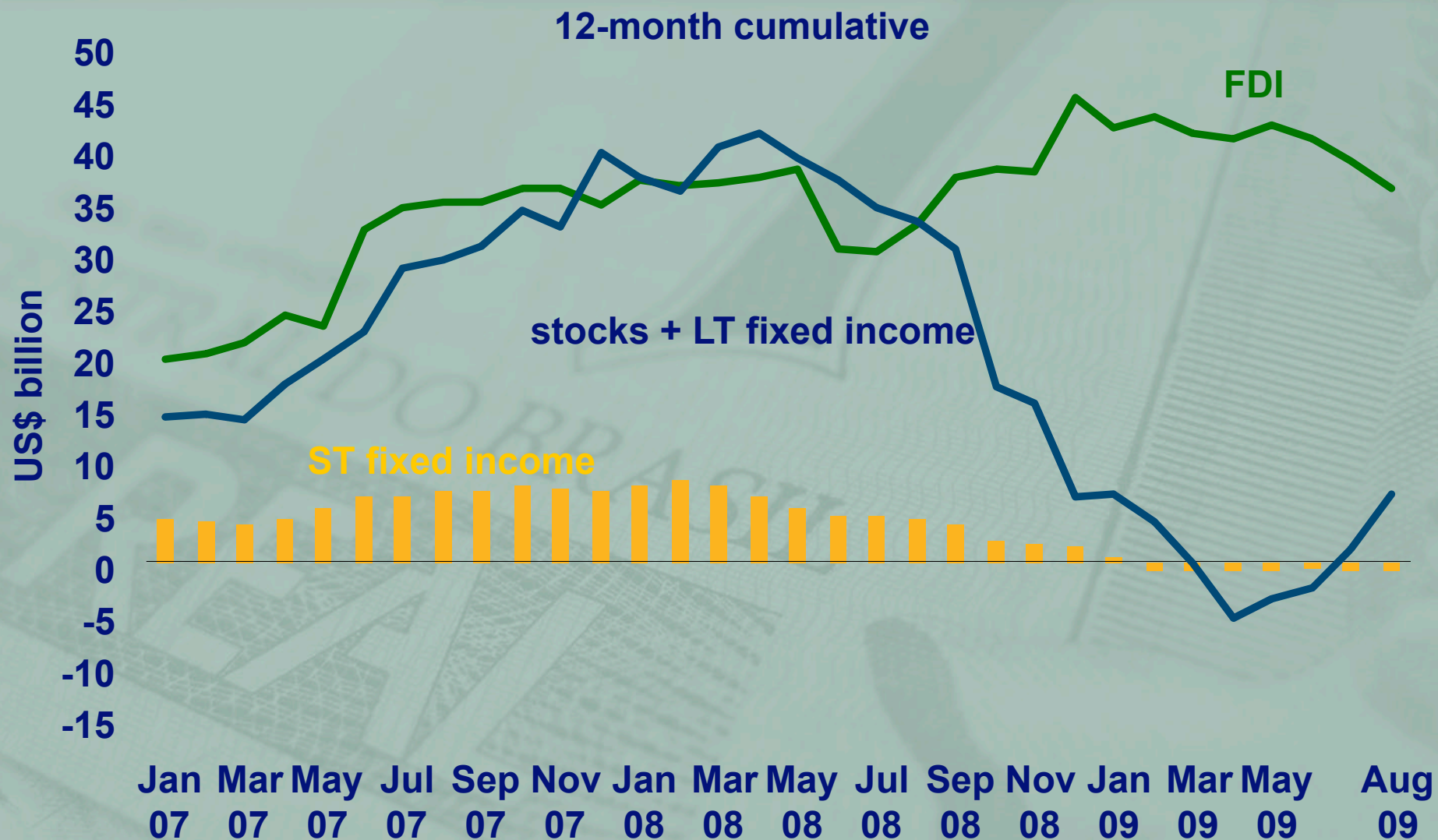


# Bank-Capital Adequacy: Basel Index

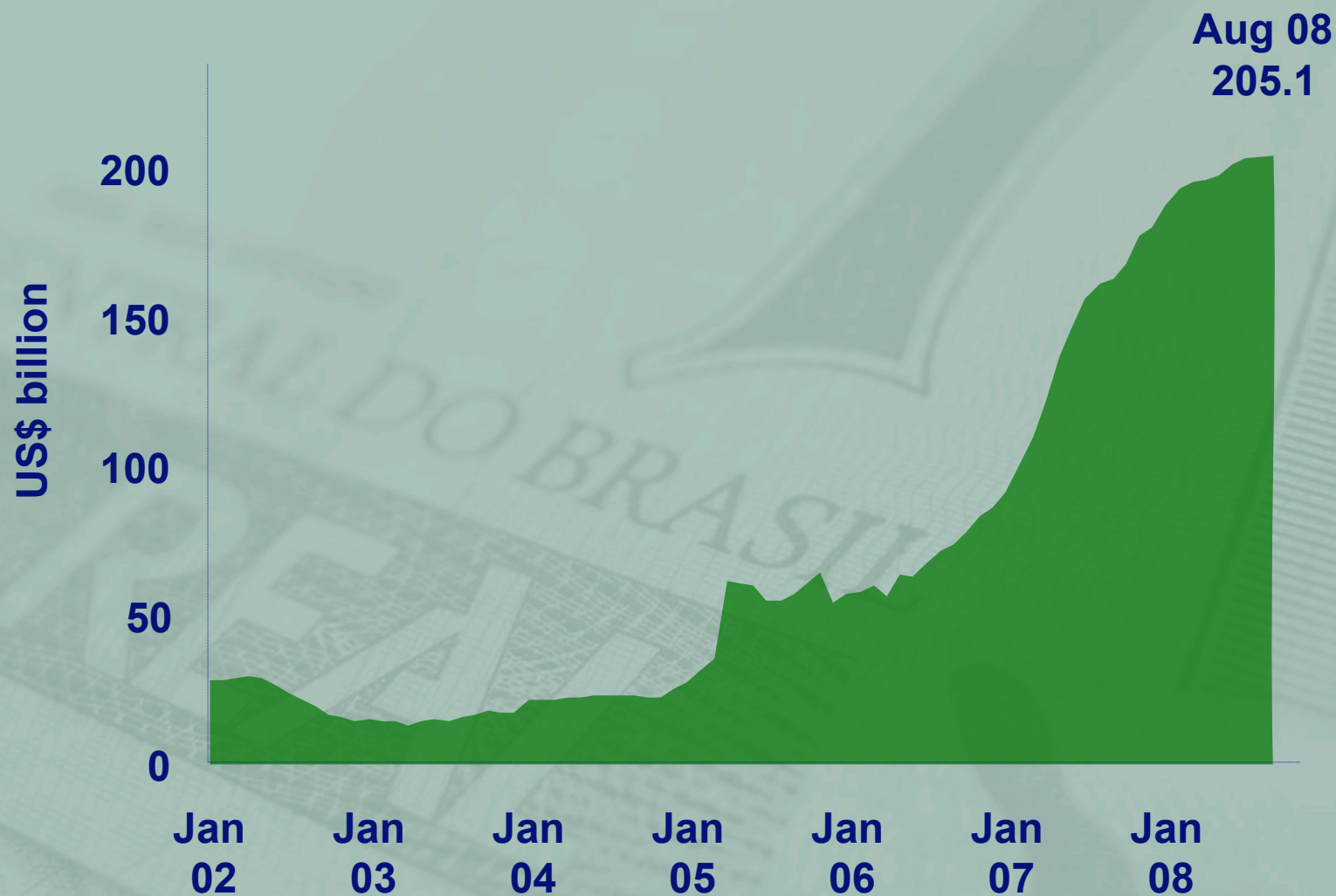
relation between capital and risk weighted assets



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



# International Reserves



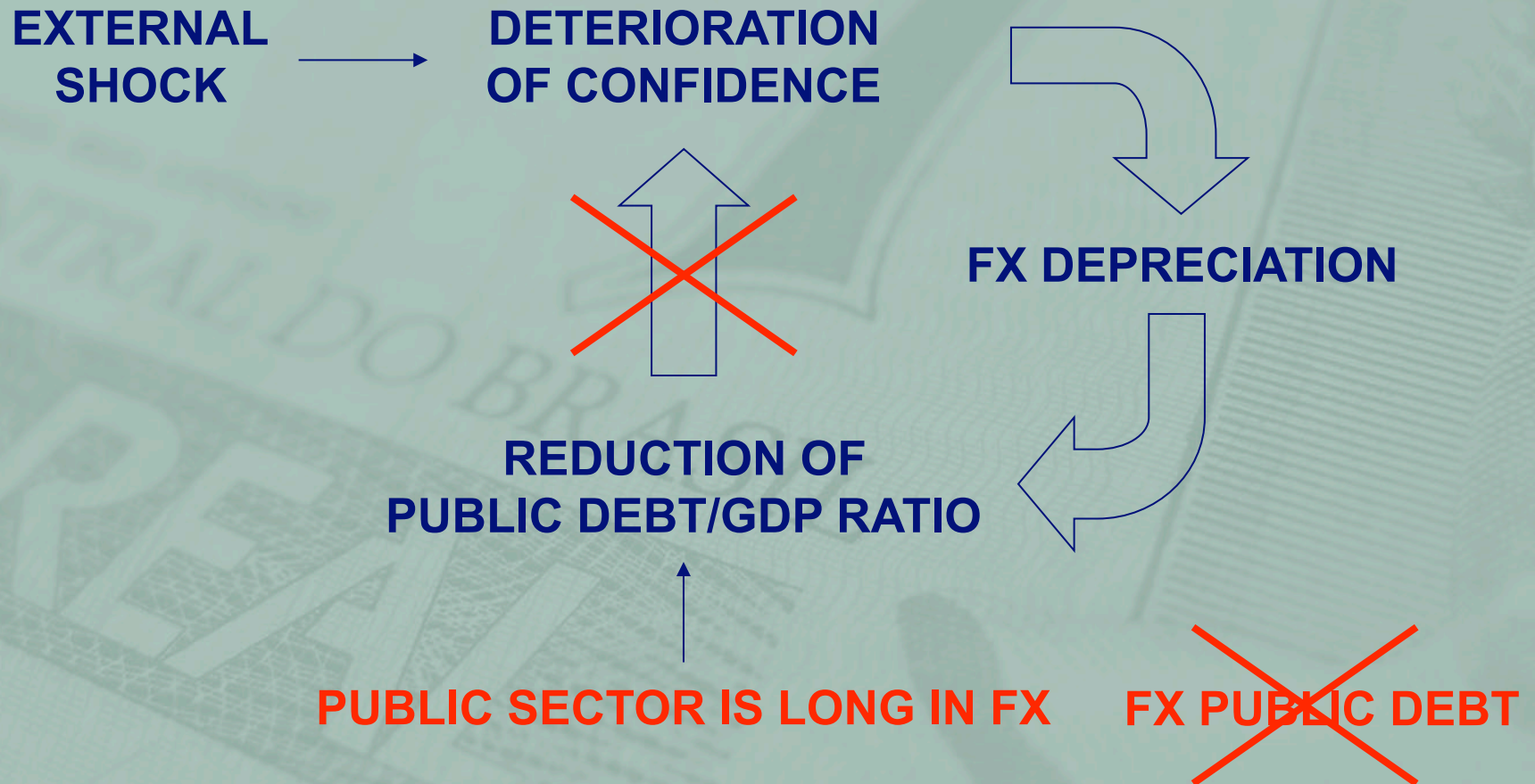
Source: Central Bank of Brazil

# Net Public External Debt



Source: Central Bank of Brazil

# External Shock Feedback Loop: Now



# Transmission of the Crisis

# Crisis – Transmission Channels



**Credit**



**External Trade**



**Confidence**

# Credit Channel

## SMALL BANKS

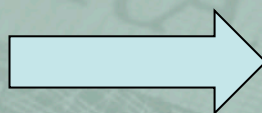
External Funding Cut  
Loss of Deposits



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

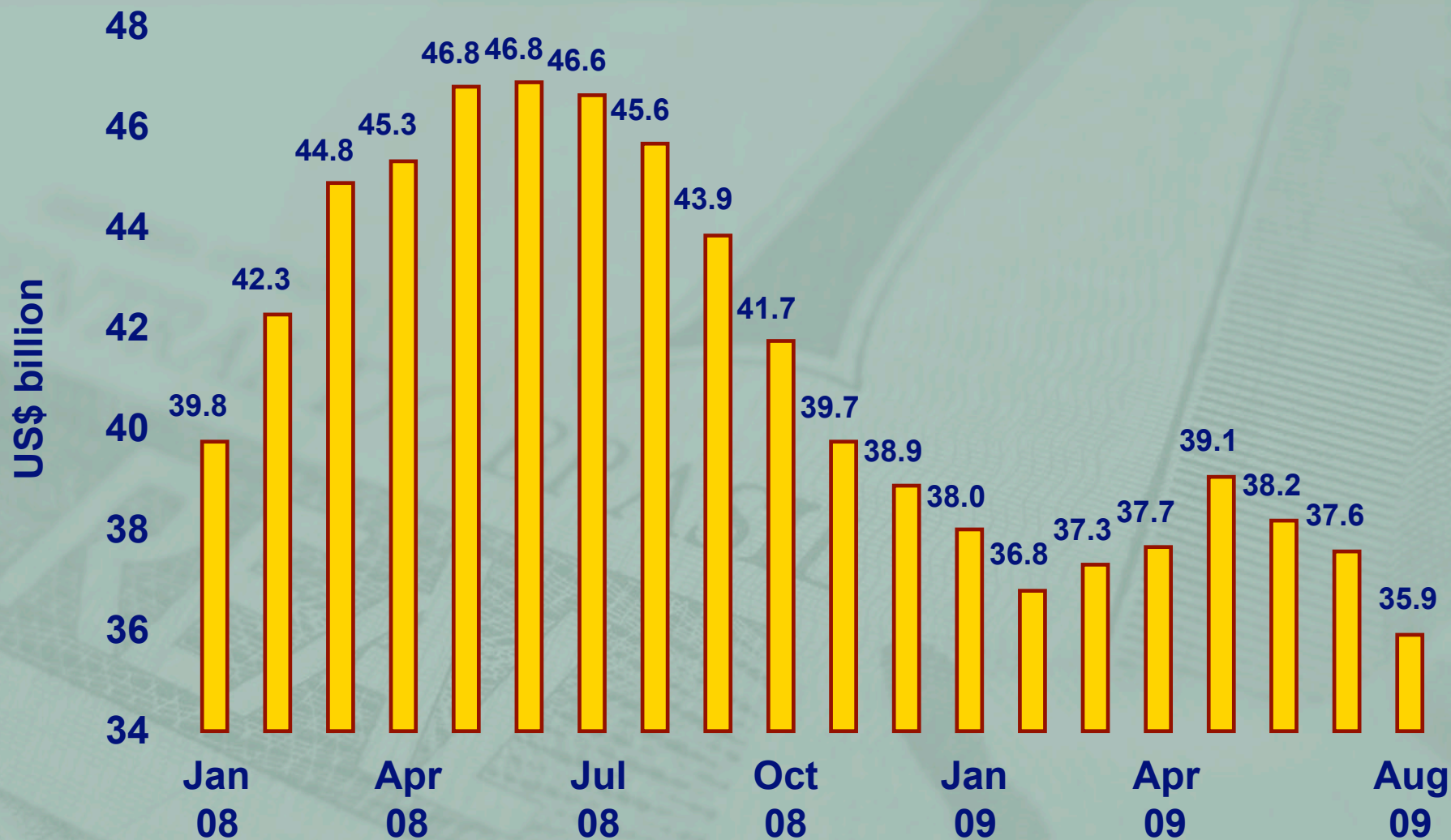
## BIG CORPORATIONS

External Credit Cut  
Loss in FX Derivatives



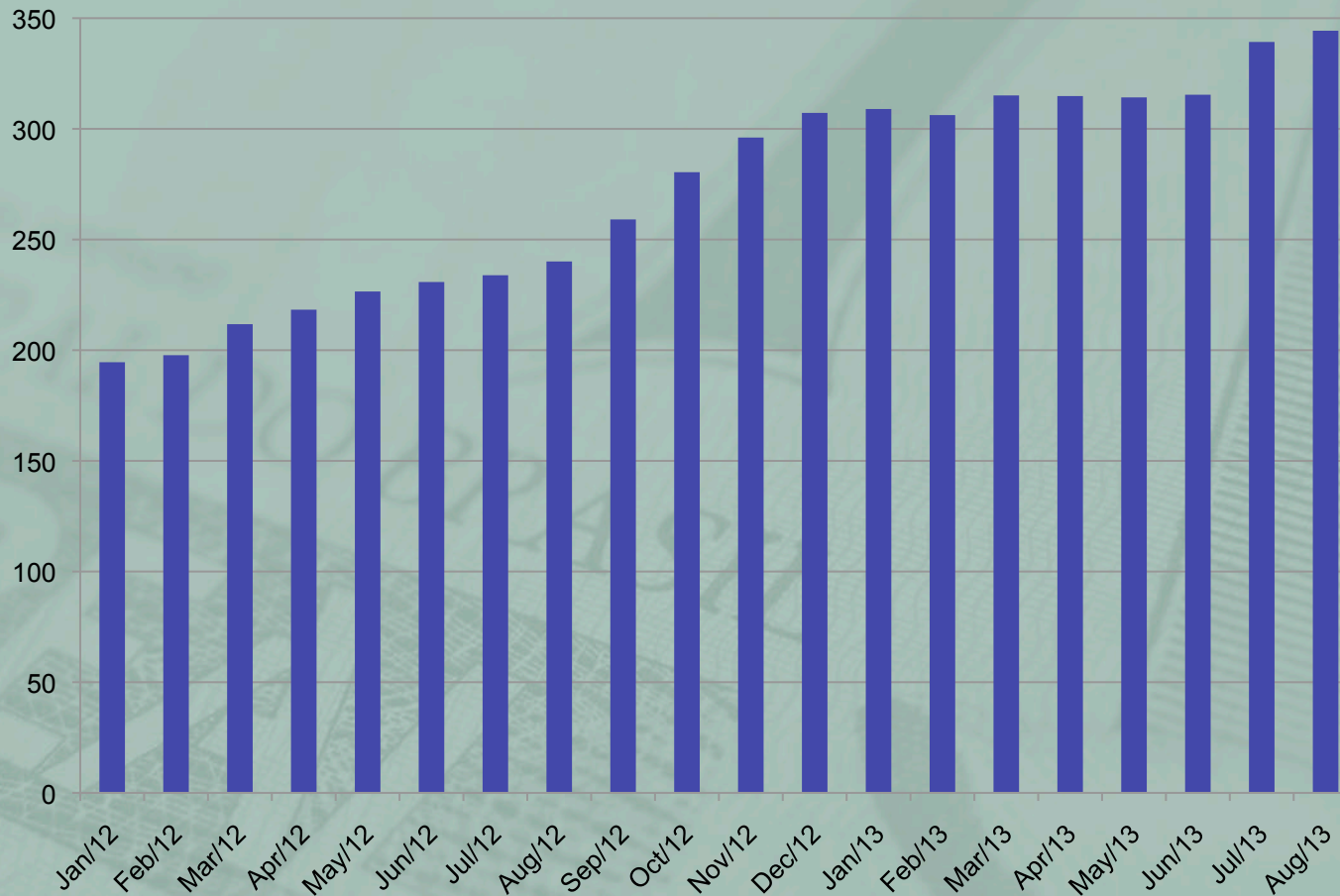
Demand for local sources  
Recession in credit sensitive

# Domestic Banking Credit with Foreign Funding

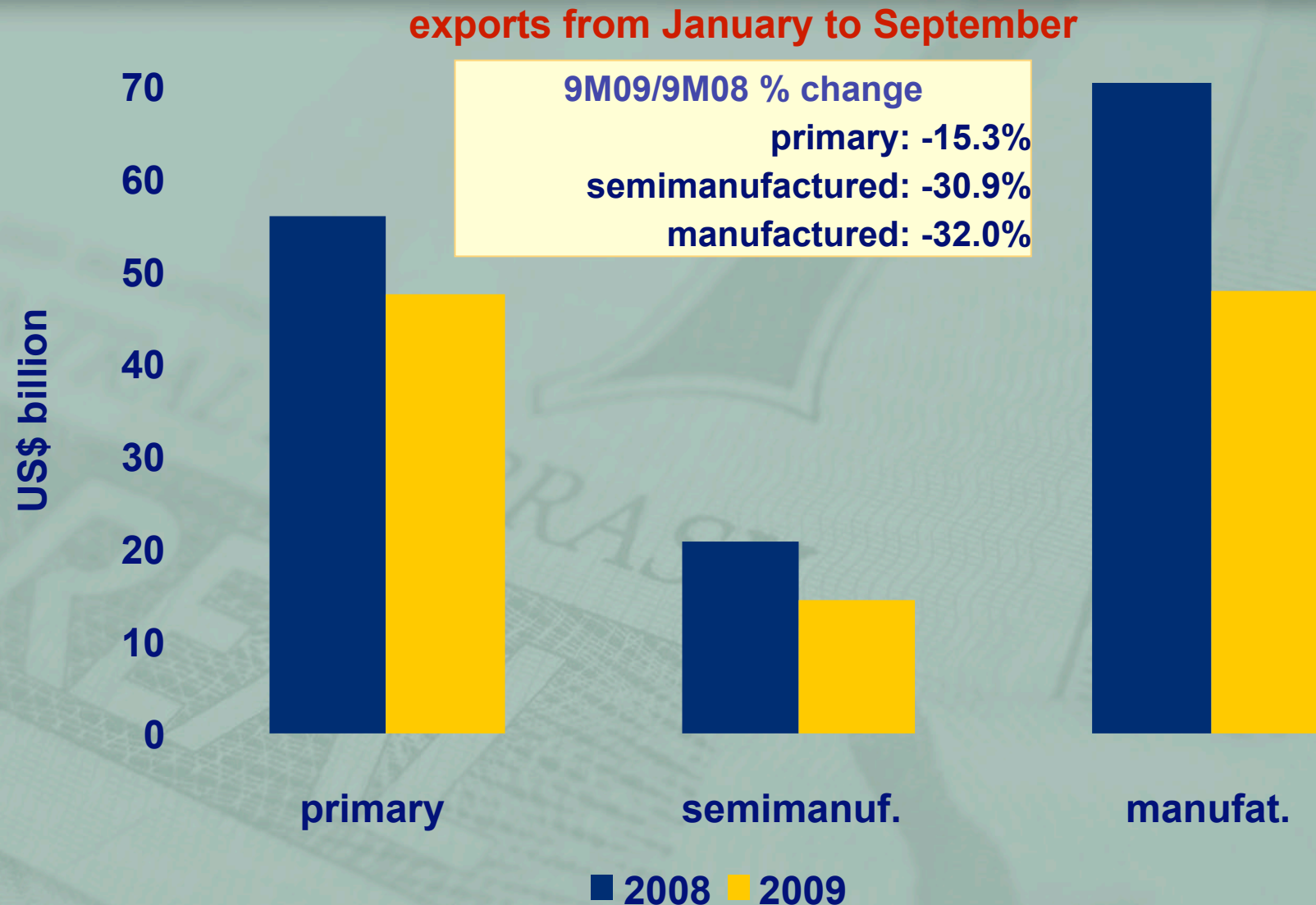


# Stock of Banking-Credit to Big Corporations

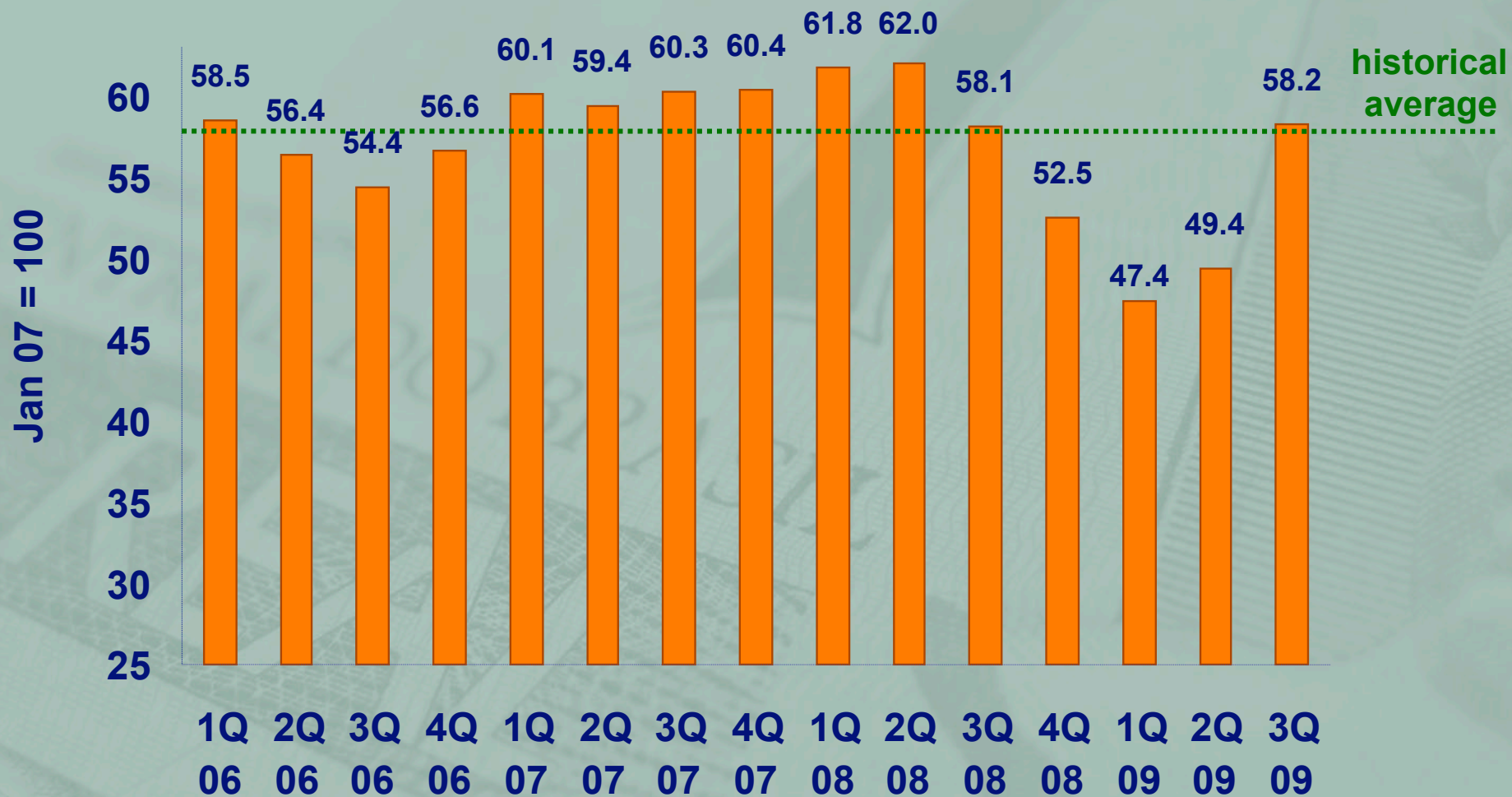
R\$ Billions



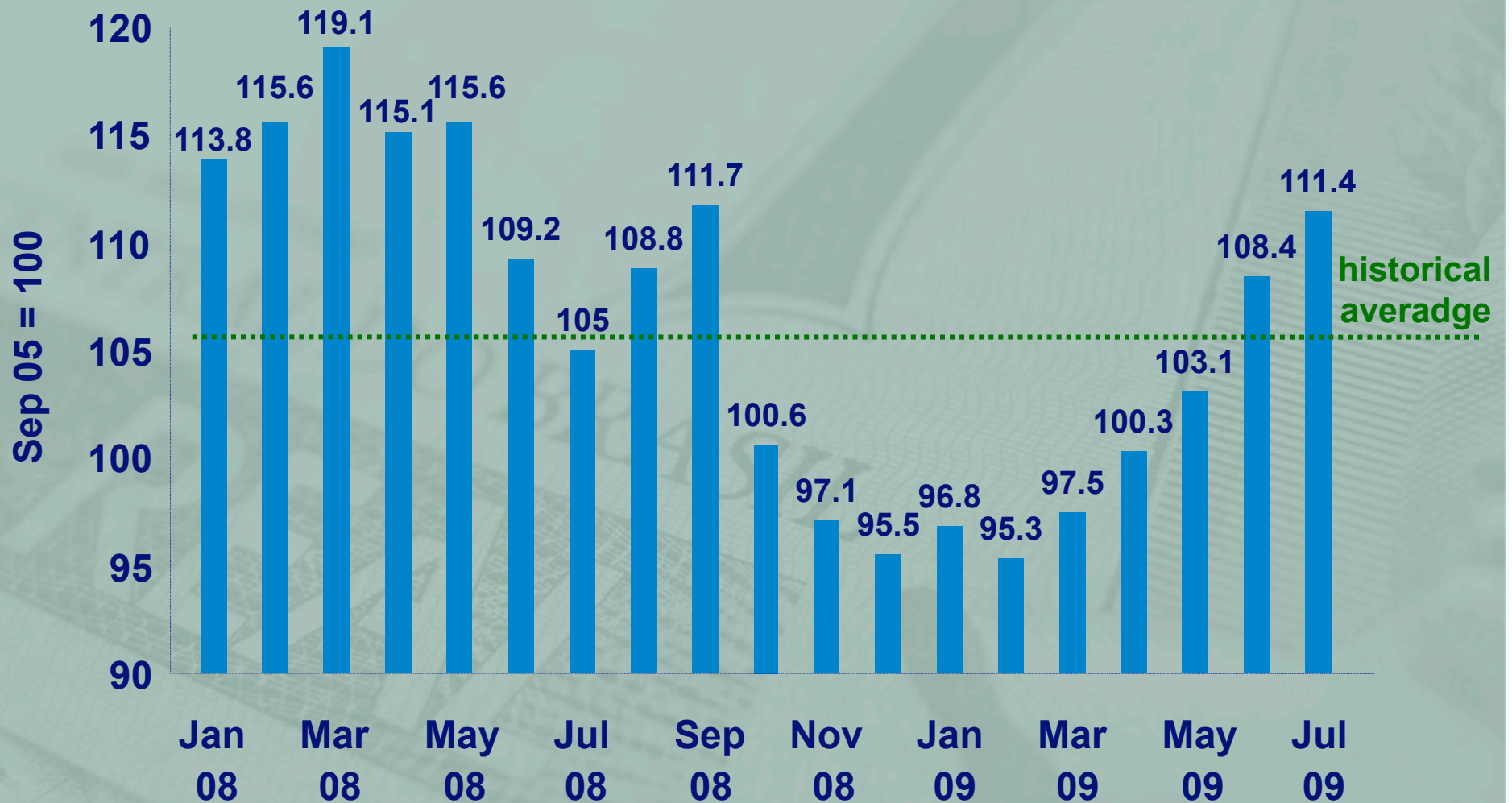
# External Trade : Impact from the Financial Crisis



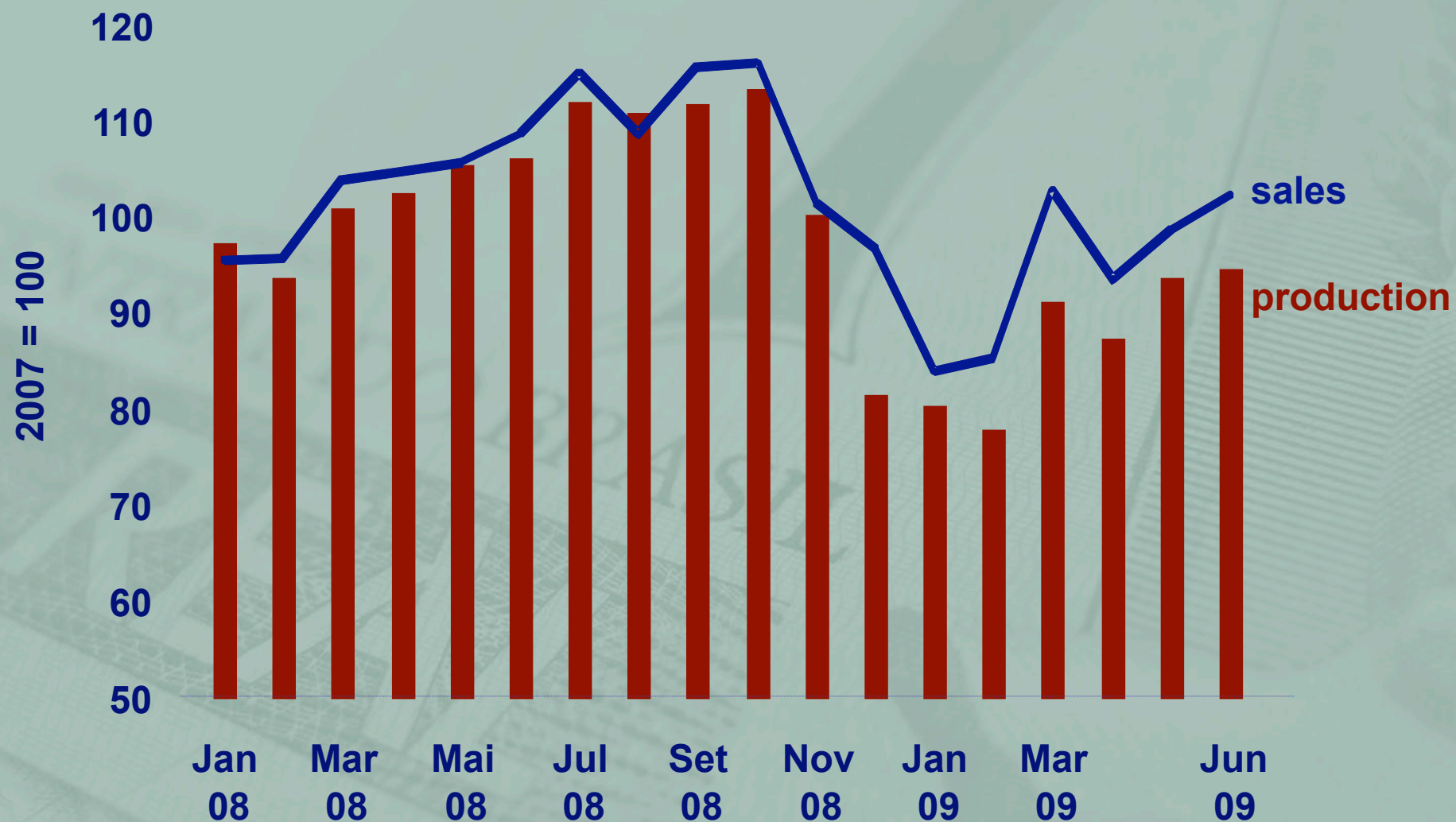
# Industrial Confidence



# 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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# **The Brazilian Reaction to the Financial Crisis**

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**¡Muchas Gracias!**