



BANCO CENTRAL DO BRASIL

Minutes of the 169th Meeting of the Monetary Policy Committee (Copom)

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Surveys and Expectations
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Date: August 28th, 2012, from 4:12PM to 18:47PM, and August 29th, from 4:56PM to 8:00PM

Place: BCB Headquarters meeting rooms – 8th floor on August 28th and 20th floor on August 29th – Brasília – DF

In attendance:

Members of the Committee

Alexandre Antonio Tombini – Governor
Aldo Luiz Mendes
Altamir Lopes
Anthero de Moraes Meirelles
Carlos Hamilton Vasconcelos Araújo
Luiz Awazu Pereira da Silva
Luiz Edson Feltrim
Sidnei Corrêa Marques

Department Heads (present on August 28th)

Adriana Soares Sales - Research Department (also present on August 29th)
Bruno Walter Coelho Saraiva – International Affairs Department
Daso Maranhão Coimbra – Department of Banking Operations and Payments System
João Henrique de Paula Freitas Simão - Open Market Operations Department
Márcio Barreira de Ayrosa Moreira - Department of Foreign Reserves
Renato Jansson Rosek – Investor Relations and Special Studies Department
Tulio José Lenti Maciel – Economic Department

Other participants (present on August 28th)

Gustavo Paul Kurrle – Press Officer
Otávio Ribeiro Damaso – Chief of Governor 's Staff

The members of the Monetary Policy Committee analyzed the recent performance of and the prospects for the Brazilian economy and for the international economy, under the monetary policy framework, which is designed to comply with the inflation targets established by the government.

Recent Economic Developments

1. Monthly inflation measured by the Extended Consumer Price Index (IPCA) rose to 0.43% in July (0.08% in June). As a consequence, twelve-month trailing inflation reached 5.20%, compared to 6.87% in July 2011. Market prices changed 5.77% in the twelve months through July (7.38% in July 2011), and regulated prices, 3.67% (5.67% in July 2011). Among market prices, the prices of tradable goods increased 3.08% in the twelve months through July (6.44% in July 2011), and the prices of non-tradable goods, 8.24% (8.18% in July 2011). The prices of food and beverages group, impacted by domestic and external weather-related factors,



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increased by 0.91% in July (-0.34% in July 2011) and reached 8.68% in twelve months. The prices of services rose 0.79% in July (0.52% in June) and 7.90% in twelve months (8.82% in July 2011). In summary, services inflation still remains at high levels and there are localized pressures in the food and beverages segment.

2. Underlying inflation measures calculated by the BCB have performed similarly to headline inflation. The average of monthly changes moved from 0.14% in June to 0.43% in July. On its turn, on a twelve-month trailing basis, the average change of the five core inflation measures moved from 5.16% in June to 5.24% in July. The smoothed trimmed means IPCA core inflation moved from 0.39% in June to 0.40% in July, and the non-smoothed trimmed means core inflation changed from 0.30% to 0.35% in the same period. Similarly, the double weight core inflation, after registering 0.07% in June, registered 0.53% in July. At the same time, core inflation by exclusion, which excludes ten household food and fuels items, increased from 0.05% in June to 0.46% in July; and the core inflation by exclusion of regulated prices and household food changed from -0.09% in June to 0.43% in July.
3. The General Price Index (IGP-DI) increased from 0.69% in June to 1.52% in July, resulting, on a twelve-month trailing basis, in 7.31 % (8.34% in July 2011). The main component of this indicator, the Wholesale Price Index (IPA), changed 7.93% in the twelve months through July, influenced by the agricultural sector (13.93%), impacted by supply shocks. According to the breakdown by stage of production, there were increases in the prices of raw materials (10.63%), intermediate goods (7.99%) and final goods (5.52%), according to the same comparison basis. Inflation measured by the Consumer Price Index (IPC), the second most important component of the IGP-DI, stood at 5.65% in the twelve months through July (6.58% in July 2011). The Civil Construction National Index (INCC), component with the lowest weight in the IGP-DI, changed 7.27%, driven by the increase in labor cost. On its turn, the Producer/Manufacturing Industry Price Index (IPP/IT), calculated by the Brazilian Institute of Geography and Statistics (IBGE), increased 1.13% in June (1.69% in May), and 6.66% in twelve months. The Copom considers that the effects of the behavior of wholesale prices on consumer inflation will depend on the current and prospective demand conditions and on the price setters' expectations regarding the future inflation path.
4. The Economic Activity Index of the BCB (IBC-Br) incorporates estimates for the monthly production of the three sectors of the economy, as well as for taxes on products, and constitutes important coincident indicator of economic activity. Considering seasonally adjusted data, the IBC-Br increased by 0.7% in June, after registering stability in May. As a consequence, the indicator increased 0.4% in the second quarter, quarter-over-quarter, and increased 0.7% year-over-year. Therefore, the twelve-month accumulated growth rate reached 1.2% in June. On its turn, the Consumer Confidence Index (ICC), from Getúlio Vargas Foundation (FGV), retreated for the fourth consecutive month in August, after reaching, in April, the record high for the series started in September 2005. On its turn, the Services Sector Confidence Index (ICS) presented the fifth consecutive decline in July and points to moderation of the activity in the sector.
5. Industrial activity registered positive growth in June after three months of declines, according to the series seasonally adjusted by the IBGE. Therefore, industrial production rose 0.2% in June, after falling 1.0% in May. Production grew in twelve of the 27 branches of activity. Industrial production fell 5.5% in June year-over-year and 2.3% on a twelve-month accumulated basis. As a consequence, production in the first semester stood 3.8% below the production in the first semester of 2011. Regarding revenues in the manufacturing industry, there was real growth of 3.1% in the first semester, according to the same comparison basis, despite a 1.4% decline in the number of hours worked, according to the National Confederation of Industry (CNI).
6. Among the industry use categories, according to data seasonally adjusted by the IBGE, the production of durable consumer goods grew 4.8% in June, the highest level in six months. The production of semi-durable and nondurable consumer goods, and of capital goods, expanded by 1.8% and 1.4%, respectively, in June, while the production of intermediate goods decreased by 0.9%. Regarding the twelve-month accumulated growth through June, there were decreases in the production of durable consumer goods (-7.6%), semi-durable and non-durable consumer goods (-0.3%), capital goods (- 5.5%) and intermediate goods (-1.5%).
7. The IBGE released the July unemployment rate for four of the six metropolitan areas covered by the Monthly Employment Survey (PME). On a month-on-month basis, the survey indicated some stability in the



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unemployment rates in Belo Horizonte, Porto Alegre and Recife, which registered 4.4%, 3.8% and 6.5%, respectively, and a sharp drop in the metropolitan region of São Paulo, where the unemployment rate decreased from 6.5% in June to 5.7% in July. Compared to July 2011, the unemployment rate fell by 0.3 percentage points (p.p.) in Belo Horizonte, 0.9 p.p. in Porto Alegre and 0.8 p.p. in São Paulo, while in Recife there was an increase of 0.2 p.p.. Data released by the Ministry of Labour and Employment (MTE) show that, in July, 142.5 thousand formal jobs were created (140.6 thousand in July 2011). The sectors that contributed the most to this increase in the number of formal jobs in the month, in absolute terms, were the services and the civil construction sectors. Also according to the PME, the average real income in July fell significantly in Belo Horizonte, Recife and São Paulo, and remained stable in Porto Alegre. In short, the set of available data indicates that, although the labor market remains robust, there are signs of moderation at the margin.

8. According to the retail monthly survey (PMC) from IBGE, broad retail sales increased 12.3% in June, year-over-year, supported, in part, by fiscal stimuli. According to the seasonally adjusted series, broad retail sales increased 6.1% in June, month-on-month, after stability in May. The accumulated growth rate in twelve months stood at 5.6% in June, with expansion in all ten sectors surveyed, with highlights for office, computer and communication material and equipment (20.9%) and furniture and appliances (14.9%). Since October 2011, the FGV, in partnership with the BCB, has been releasing the Trade Confidence Index (ICOM). This indicator provides important additional information, as it portrays the current outlook and signals the evolution of commercial activity in a more timely manner. In July, the index declined, after remaining stable in June. For the upcoming months, the retail sales trajectory will continue to be influenced by governmental transfers, by the pace of real payroll growth, by the reduction in borrowing costs and by moderate credit expansion.
9. The installed capacity utilization rate (Nuci) in the manufacturing industry, calculated by the FGV, without seasonal adjustment, rose in August (84.4%), standing 0.4 p.p. above the level observed in August 2011. According to the seasonally adjusted series calculated by the FGV, the Nuci stood at 84.0% in August, also 0.4 p.p. above the level recorded in August 2011 and 2.7 p.p. below the record high of the series recorded in June 2008. Capacity utilization intensified in the consumer goods sector, which reached 86.1%, and also recovered in the capital goods sector, which recorded 82.6%. In the sector of intermediate goods and construction inputs, the levels stood at 85.5% and 87.0%, respectively. Also according to the FGV, the Industry Confidence Index continued a gradual recovery trajectory, reaching the highest level since July 2011 according to the seasonally adjusted series, due to improvements in perceptions of both the current situation and expectations. The share of companies that reported inventories at normal levels increased since the last Copom meeting.
10. The trade balance surplus on a twelve-month accumulated basis continued a downward trajectory, dropping to US\$23.6 billion in July. This result stemmed from US\$253.7 billion in exports and US\$230.1 billion in imports, associated to changes of 7.7% and 10.3%, respectively, compared to the previous twelve months. As a consequence, the current account deficit in the same period increased from US\$51.8 billion in June to US\$52.0 billion in July, equivalent to 2.17% of GDP. On its turn, foreign direct investment totaled US\$66.3 billion in the twelve months through July, equivalent to 2.77% of GDP, surpassing the need for external financing.
11. Global economy faces a period of above-than-usual uncertainty, with prospects of low growth for a prolonged period. In this sense, a moderate pace of activity in the United States (US) prevails, in an environment of risks deriving from the fiscal restraint outlook and from the European crisis. High unemployment rates for a long period, coupled with the implementation of fiscal adjustments, the limited space for countercyclical actions and political uncertainties are translated into projections of low growth for mature economies. The composite leading indicator released by the Organization for Economic Cooperation and Development (OECD), referring to June, indicates moderate growth or strong slowdown in the main economies. In the same sense, the disaggregated indicators of the Purchasing Managers Index (PMI) for July suggest moderate global activity, with slowdown in manufacturing activity. Regarding monetary policy, advanced economies persist with strongly accommodative stances, which can eventually be deepened further. Core inflation measures have remained at moderate levels in the US, in the Euro Area and in Japan. In emerging economies, in general, the monetary policy bias is expansionist, which combines, in some cases, with additional countercyclical policies.



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12. The price of Brent oil barrel has increased since the last Copom meeting and breached US\$110. It bears highlighting that the even higher geopolitical complexity that involves the oil sector tends to heighten the volatile behavior of prices, which is also a reflex of the low predictability of some global demand components and of the dependency of supply growth on long term risky investment projects. As measured by the Commodity Research Bureau (CRB), since the last Copom meeting, international prices of metallic and agricultural commodities have increased 7.8% and 1.0%, respectively. Therefore, relative to the record highs observed in April 2011, the changes reach -23.4% and -10.0%, respectively. On its turn, the Food Price Index, calculated by the Food and Agriculture Organization of the United Nations (FAO), accumulates a fall of 10.5% until July, compared to the peak recorded in February 2011. In the recent past, the high volatility observed for the commodities prices was influenced by the abundant global liquidity, in a context where financial markets adjust to new expectations for growth and volatility in FX markets. Prospectively, it is plausible to affirm that the reduction of growth targets in China, coupled with the fragility of the global economy, tends to generate downward pressures over commodities prices in the medium run.

Assessment of Inflation Trends

13. The identified shocks, and their impacts, were reassessed according to the new set of available information. The scenario considered in the simulations was based on the following assumptions:
 - a) the projected adjustments for gasoline and bottled gas prices, for 2012, were maintained at 0%, the same value considered at the July Copom meeting;
 - b) the projected adjustments for 2012 for fixed telephone and for electricity were maintained at -1.0% and 1.4%, unchanged relative to the July meeting;
 - c) the projected adjustment, based on individual items, for the set of regulated prices inflation accumulated in 2012, was maintained at 3.6%, considered at the July Copom meeting; and
 - d) the projected adjustment for the set of regulated prices inflation accumulated in 2013 was maintained at 4.5%, the same value considered at the July Copom meeting. Such projection is based on endogenous determination models for regulated prices, which compute, among other factors, seasonal components, market prices inflation, and the IGP (General Price Index) change.
14. The projection for the spreads over the Selic rate, based on the 360-day swap rates, on the benchmark scenario, estimates -24 bps and 23 bps spreads in the fourth quarter of 2012 and 2013, respectively.
15. Regarding fiscal policy, projections assume the achievement in 2012 of the public sector primary surplus around 3.10% of GDP, without adjustments. Furthermore, it is accepted, as a working hypothesis, a primary surplus around 3.10% of GDP for 2013, without adjustments, according to parameters set out in the Budget Guidelines Law (LDO) - 2013. For 2014, it is accepted, as a working hypothesis, a primary surplus of 3.10% of GDP, without adjustments.
16. The set of projections incorporated the estimated effects of the reduction in the neutral interest rate identified over the last years.
17. The main scenario does not include the occurrence of extreme events in international financial markets, but considers the estimates of the impacts caused by changes in the external environment on the Brazilian economy. In particular, it incorporates the estimated effect of the recent supply shock in agricultural commodities.
18. Since the last Copom meeting, the median of the expectations compiled by the BCB's Investor Relations and Special Studies Department (Gerin) for the 2012 IPCA increased from 4.85% to 5.19%. For 2013, the median of inflation expectations was maintained at 5.50%. Specifically for banks, asset managers and other institutions (real sector companies, brokers, consultancies and others), the median of expectations for the 2012 IPCA changed to 5.20%, 5.19% and 5.19% from 4.87%, 4.85% and 4.85%, respectively. For 2013, the median changed to 5.50%, 5.67% and 5.46% from 5.50%, 5.70% and 5.46%, in the same order.



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19. The benchmark scenario assumes the maintenance of the exchange rate at R\$2.00/US\$1.00 and the Selic rate at 8.00% p.y. during the forecast period. Under this scenario, the projection for the 2012 inflation increased relative to the figure considered at the July Copom meeting and it stands above the 4.50% midpoint target established by the National Monetary Council (CMN). According to the market scenario, which incorporates the consensus exchange and Selic rates trajectories collected by Gerin in the period immediately prior to the Copom meeting, IPCA inflation forecast for 2012 increased and it stands above the midpoint inflation target. For 2013, the inflation projection remained stable in both scenarios, above the midpoint target also in both cases. For the first half of 2014, the inflation forecast is above the midpoint inflation target in both scenarios.

Monetary Policy Decision

20. The Copom evaluates that monetary policy should contribute to the consolidation of a favorable longer-term macroeconomic environment. In this respect, the Copom reassures that, under the inflation targeting regime, it guides its decisions according to BCB projected inflation and based on the analysis of alternative scenarios for the evolution of the main variables that determine prices dynamics. The Committee also understands that low risks for the underlying inflation in the short run tend to reduce uncertainties regarding the future behavior of headline inflation, facilitate the assessment of scenarios by the monetary authority, as well as help the process of coordination of economic agents' expectations, particularly price setters'. Additionally, it is noteworthy that low risks for the underlying inflation in the short run tend to intensify the effects of monetary policy actions, enabling them to affect in a more long-lasting manner the dynamics of headline inflation in the future. Although the Copom recognizes that other macroeconomic policy actions may influence the prices trajectory, it reaffirms its view that it is particularly under the responsibility of the monetary policy to remain especially vigilant to guarantee that pressures detected in shorter horizons do not spread to longer horizons.
21. International evidence, ratified by the Brazilian experience, indicates that high inflation rates lead to the increase in risk premia, both for private and public funding, and to the shortening of planning horizons, both for households and companies. Consequently, high inflation rates reduce investments and economic growth potential, in addition to presenting regressive effects on income distribution. In other words, high inflation rates do not originate any lasting results for economic and employment growth; on the contrary, they create permanent damage to these variables in the medium and long terms. Therefore, the strategy adopted by the Copom aims to ensure the convergence of inflation towards the targets path, which requires that possible deviations from the target path be promptly corrected. Such strategy takes into account the time lags in the transmission mechanism and is the most adequate to deal with the uncertainty inherent to the process of monetary policy formulation and implementation.
22. The Copom considers that, since its last meeting, the risks to global financial stability have remained high, particularly those deriving from the ongoing deleveraging process observed in the main economic blocks. The Committee understands that, overall, the prospects of moderate global activity have remained unchanged, and the restrictions to which several mature economies were exposed have changed little. It also notes that, in these economies, there seems to be limited leeway for monetary policy actions, and a scenario of fiscal restraint also prevails, in this and in the upcoming years. Moreover, in important emerging economies, despite the resilience of domestic demand, the pace of activity remained moderate. On the other hand, since the last meeting, there were evidences of localized pricing pressures, stemming from an unfavorable supply shock in agricultural commodities. For the Committee, this shock tends to be less intense and less lasting than the one observed in 2010/2011, as well as it tends to reverse in the medium term. Therefore, despite manifesting inflationary bias in the short term, the international scenario looks disinflationary in the medium term.
23. For the Copom, there are cumulative evidences supporting the view that the transmission of external developments to the Brazilian economy materializes through several channels, among others, moderation of total trade, moderation in investment flows and tighter credit conditions. Another transmission channel of great importance is the impact over businessmen confidence.
24. The Copom evaluates that, although domestic demand expansion has moderated, prospects for economic activity in this and in the upcoming semesters are favorable, with some asymmetry among the several sectors.



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This assessment is supported by signs that point to moderate expansion of credit supply, both for individuals and corporate, and by the fact that consumers' and, to a lesser extent, businessmen's confidence stands at high levels. The Committee understands, additionally, that the domestic activity will continue to be benefited by public transfers, as well as by the labor market vigor, mirrored in historically low unemployment rates and in wages growth, despite some accommodation at the margin.

25. The Copom reaffirms its view that inflation accumulated in twelve months, which started to retreat in the last quarter of 2011, tends to move non-linearly towards the targets path. The Committee evaluates that the reversion in the inflation trend will contribute to improve the economic agents' expectations, especially price setters', about the inflation dynamics in this and in the upcoming semesters.
26. The Copom notes that the main inflation scenario considers the materialization of the assumed trajectories regarding fiscal variables. It bears highlighting that the generation of primary surpluses in line with the hypotheses considered for inflation projections, in addition to contributing to reduce the mismatch between supply and demand growth rates, will strengthen the reduction trend of the public debt-to-GDP ratio and the positive perception regarding the macroeconomic environment in the medium and long terms.
27. The Copom highlights that its main scenario also considers moderate expansion in the credit market. Still about the credit market, the Committee considers opportune the initiatives with the aim of moderating the concession of subsidies through credit operations.
28. The Copom evaluates as decreasing the risks stemming from the persistence of the mismatch, in specific segments, between supply and demand growth rates. However, it highlights the narrow idleness margin in the labor market, despite the signs of moderation in this market, and considers that, under such circumstances, an important risk stems from the possibility of concession of wages increases incompatible with productivity growth and their negative impacts over inflation dynamics. On the other hand, the Copom notes that the level of installed capacity utilization has stabilized and is below the long-term trend, in other words, it is contributing to the opening of the output gap and to contain prices pressures. The Committee also highlights risks stemming from the instability in the prices of *in natura* products and grains, which manifest, for example, in the dynamics of wholesale prices.
29. The Committee considers that the recovery in domestic economic activity has materialized gradually; on the other hand, it highlights that the main scenario encompasses more intense pace of activity in this semester and next year. The Committee identifies decrease in the probability of extreme events in international financial markets, but, at the same time, it argues that the external environment remains complex, given the lack of a final solution for the European financial crisis, and the risks associated to the ongoing deleveraging process – of banks, households and government - in the main economic blocks. Since the last Committee meeting, although the inflation prospective scenario has been negatively impacted by supply shocks related to domestic and foreign climatic events in the short term, it maintained favorable signs for longer periods. Thus, the Committee also notes that, according to the main scenario adopted, inflation tends to move towards the target path.
30. In this context, the Copom unanimously decided to reduce the Selic rate to 7.50% p.a., without bias.
31. The following members of the Committee voted for this action: Alexandre Antonio Tombini, Governor, Aldo Luiz Mendes, Altamir Lopes, Anthero de Moraes Meirelles, Carlos Hamilton Vasconcelos Araújo, Luiz Awazu Pereira da Silva, Luiz Edson Feltrim and Sidnei Corrêa Marques.
32. The Copom evaluates that domestic demand tends to show robustness, especially household consumption, largely due to the effects of stimulus factors, such as income growth and moderate credit expansion. This scenario tends to prevail in this and in the upcoming semesters, when domestic demand will be impacted by the effects of monetary policy actions recently implemented, which are, in short, lagged and cumulative. For the Committee, these effects, the programs of public services concession and the gradual recovery of confidence create good prospects for investment in this and in the upcoming semesters. The Committee considers that recent initiatives indicate scenario of neutrality of the public sector results. The Committee also



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notes that the fragile international scenario represents as an important factor restraining aggregate demand. These elements and quasi fiscal developments are important parts of the context in which future monetary policy decisions will be taken, aiming to ensure the timely convergence of inflation to the targets path.

33. The Copom understands that the Brazilian economy has experienced significant structural changes, which determined retreat in the interest rates in general and, in particular, in the neutral rate. Among the factors that support this view, it bears highlighting the reduction of risk premia, a direct consequence of the accomplishment of the inflation target for the eighth consecutive year, of the macroeconomic stability and of institutional improvements. Moreover, the process of interest rates reduction was favored by changes in the structure of the financial and capital markets, by the credit market deepening, as well as by the generation of primary surpluses consistent with the maintenance of decreasing trend for the public debt-to-GDP ratio. For the Committee, all these changes are characterized by a high degree of persistence – although, due to the economic cycles themselves, specific and temporary reversions may occur – and contribute for the Brazilian economy's current solid indicators of solvency and liquidity.
34. The Copom also considers that the increase in the supply of external savings and the reduction of its funding cost have contributed to the reduction of the domestic interest rates, including the neutral rate, which, according to the Committee's assessment, are largely permanent developments.
35. In light of the above, considering the cumulative and lagged effects of policy actions implemented until the moment, which in part reflect in the ongoing recovery of economic activity, the Copom understands that, if the prospective scenario justifies an additional adjustment in monetary conditions, this movement should be conducted with extreme parsimony.
36. At the end of the meeting, it was announced that the Committee will reconvene on October 9th, 2012, for the technical presentations, and on the following day, to discuss monetary policy, as established in the Communiqué 21,213 of June 29th, 2011.

SUMMARY OF DATA ANALYZED BY THE COPOM

Inflation

37. The IPCA-15 rose 0.39% in August, up from 0.33% in July, totaling 3.32% in the year and 5.37% in twelve months, compared to 5.24% in the twelve months through July, according to data released by the IBGE. The monthly result reflected acceleration in market and regulated prices. Regarding market prices, which increased 0.45% in August, compared to 0.41% in July, the movement was influenced by the behavior in the prices of tradable goods, which increased from -0.02% to 0.22%, while the prices of non-tradable goods decelerated to 0.66%, down from 0.79%, favored by the lesser pressure in the rate relative to services prices, which increased 0.61% in August, down from 0.76% in July. Regulated prices rose 0.19% in August, up from 0.09% in July. The transportation group, which showed a negative change of 0.59% in July, was the main responsible for the acceleration of the index in August, reporting price stability in the month. The diffusion index stood at 65.75% in August, up from 61.64% in July.
38. On a twelve-month basis through August, market and regulated prices accelerated in relation to July from 5.72% to 5.84% and from 3.98% to 4.08%, respectively. The evolution of market prices reflected the effect of the acceleration in the prices of the non-tradable goods, from 7.73% to 8.05%, while the prices of the tradable goods decelerated, from 3.50% to 3.40%. The prices of the services segment increased 7.62% in the last twelve months through August, compared to 7.46% and 7.19%, in the corresponding periods through July and June.
39. The IGP-10 changed 1.59% in August, after increasing 0.96% in July, according to the FGV, with acceleration in the IPA and IPC, while the INCC recorded deceleration in the month. The index accumulates an increase of 5.49% in the year and 7.50% in twelve months.



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40. The IPA-10 changed 2.21% in the month, compared to 1.24% in July, totaling 6.05% in the year and 8.18% in twelve months. The prices of agricultural and livestock products increased 6.23% in August, up from 1.94% in the previous month, totaling 12.42% in the year and 15.02% in twelve months. The prices of industrial products increased 0.72% in the month, down from 0.99% in July, totaling 3.77% in the year and 5.74% in twelve months. The monthly performance of prices of agricultural and livestock products evidenced, in particular, the change registered in the prices of soybeans (15.62%), corn (22.17%), coffee (9.25%) and tomato (51.09%), with respective contributions of 0.87 p.p., 0.50 p.p., 0.13 p.p. and 0.12 p.p. for the IPA-10 result. Among the prices of industrial products, the main influences were exerted by vegetable oils and fats, and petroleum and alcohol derivatives, with respective increases of 11.72% and 2.38%, and individual contributions of 0.35 p.p. and 0.18 p.p. to the monthly index.
41. The IPC-10 increased 0.29% in August, compared to 0.19% in July, totaling 3.64% in the year and 5.64% in twelve months. The IPC-10 change in August was mainly influenced by the 1.11% increase in the food group, which contributed 0.26 p.p. to the monthly index, and by the decline registered in the transportation group, with change and contribution to the index of -0.44% and -0.08 p.p., respectively. The INCC-10 changed 0.49% in the month, down from 0.84% in the previous month, as a result of the decelerations in the costs of labor force (from 1.17% to 0.52%) and in the prices of materials, equipment and services (from 0.50% to 0.47%). The INCC-10 accumulated changes of 6.00% in the year and 7.25% in the twelve months through August.
42. The IPP/IT increased 1.13% in June, after increasing 1.69% in May. In the year, the IPP/IT increased 4.53%, compared to 0.56% in the same period of 2011, and increased 6.66% in the last twelve months through June, compared to 4.78% in the previous month. The monthly result of IPP/IT was mainly influenced by the increases in the prices related to the industries of food products and other chemical products, with respective contributions of 0.45 p.p. and 0.17 p.p. to the index. The index change in the twelve months through June reflected, mainly, elevations related to the contributions stemming from the industries of food products, 3.12 p.p., and other chemical products, 0.62 p.p., offset by the contributions of textiles, -0.09 p.p., and metallurgy industry, -0.03 p.p..
43. The Commodity Index Brazil (IC-Br) increased 7.81% in July, reflecting respective changes of 10.37%, 6.06% and -1.76% related to the segments of agriculture and livestock, energy and metal, respectively. In the year, the index accumulates an increase of 8.71%, with increases of 10.92%, 0.86% and 5.26%, in the same order. In the last twelve months through July, the index accumulated an increase of 12.27%, with increases of 17.16% in the sub-index composed by agricultural products, and 6.75% in the sub-index related to energy commodities, while the one related to metallic commodities decreased 3.89% in the period.

Economic Activity

44. The Economic Activity Index of the BCB (IBC-Br) increased 0.75% in June, month-on-month, considering seasonally adjusted data. In the second quarter, the index increased 0.38%, over the first quarter, when it had increased 0.62%, according to the same comparison basis. Considering observed data, the IBC-Br increased 0.99% in June, year-over-year, compared to the increase of 1.09% in May, according to the same comparison basis. The index increased 0.87% in the year and 1.20% in the twelve months through June.
45. Broad retail sales, which include vehicles and construction inputs, increased 6.1% in June, month-on-month, according to data seasonally adjusted from the IBGE's retail monthly survey (PMC), after stability in May and increase of 0.8% in April. With this result, broad retail sales grew 3% in the second quarter, quarter-over-quarter. By segment, nine out of the ten surveyed segments increased, with highlights for the increase of 16.4% in vehicles, motorcycles, parts and pieces, opposing to the decrease of 8.9% in office, computer and communication material and equipment. In the year, broad retail sales increased 7%. Retail sales volume increased 1.5% in June, month-on-month seasonally adjusted, after decrease of 0.8% in May and increase of 0.7% in April, according to the same comparison basis. Considering seasonally adjusted data, there was expansion of 0.8% quarter-over-quarter, 9.1% in the year and 7.5% in twelve months.
46. Considering observed data, broad retail sales increased 12.3% in June, year-over-year, with expansion in nine segments, with highlights for the sales of vehicles, motorcycles, parts and pieces (19.8%); and furniture and



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household appliances (15.8%); whereas office, computer and communication material and equipment decreased 14.6%. In the twelve months through June, broad retail sales increased 5.6%, mainly driven by increases in the sales of office, computer and communication material and equipment (20.9%), furniture and household appliances (14.9%); and pharmaceutical, medical, orthopedic, perfumery and cosmetics articles (9.9%).

47. Automobile sales by dealers, including cars, light commercial vehicles, trucks and buses, decreased 5.3% in July, month-on-month, after increases of 35% in June and 2.4% in May, according to the Brazilian Federation of Automobile Vehicles Distribution (Fenabrave) data, seasonally adjusted by the BCB. The sales reached 364.2 thousand units, a record high for the month of July and the second record high for the historical series, reflecting the tax exemption implemented by the federal government in the end of May. Automobile vehicles sales increased 1.9% in the year, as a consequence of the increase of the sales of cars (4%), while the sales of trucks and buses fell by 18.4% and 12.2%. Light commercial vehicles sales remained stable, according to this comparison basis.
48. Capital goods imports quantum index, released by the Foreign Trade Studies Centre Foundation (Funcex) and seasonally adjusted by the BCB, decreased 8.7% in July, month-on-month. According to the observed data, the index decreased 2.1% year-over-year, increased 2.8% in the year and 3.1% in the twelve months through July.
49. Capital goods production increased 1.4% in June, accumulating a 3.6% increase in the quarter, compared to the one ended in March, according to data seasonally adjusted from the Monthly Industrial Survey (PIM) by the IBGE. The performance of the category stemmed from the increase in the production of equipment for electrical energy (6.3%) and agricultural capital goods (5.9%), as opposed to the decrease in the production of agricultural pieces (-14,6%); capital goods for non-industrial series use (-4,1%) and mixed-use equipments (-3,6%).
50. Construction inputs production decreased by 3.2% in June, accumulating an increase of 0.1% in the quarter, quarter-over-quarter, considering seasonally adjusted data. Compared to the same periods of 2011, the segment production decreased 2.7% in the month, and increased 2.4% in the year and 3.3% in twelve months.
51. Disbursements granted by the Brazilian Development Bank (BNDES) totaled R\$139.3 billion in the twelve months through May, 15.9% below the one registered in the same period of 2011, as a consequence of the retraction of 50% in funding for the manufacturing industry. In the period, the infrastructure sector absorbed 40% of the total funds released, followed by industry, 30%, commerce and services, 23%, and agriculture and livestock, 7%.
52. Industrial production increased 0.2% in June, according to IBGE seasonally adjusted data, after a 1% decrease (revised) in May, reflecting expansion of 0.4% in manufacturing industry and retreat of 2.2% in mining. By use categories, it bears highlighting the increase of 4.8% in the durable goods production, 1.8% in the production of semi and non-durable consumer goods and 1.4% in capital goods, whereas the production of intermediate goods decreased 0.9%. Twelve out of the 26 manufacturing industry activities surveyed increased in the month, with highlights for the segments of other transportation equipment (12.5%); pharmaceutical (8.6%); and electronic material and communication equipment (8%). On the other hand, the segments of medical-hospital instrumentation equipment and also rubber and plastic products recorded the largest monthly retraction, 10.9% and 5.7%, respectively. The industrial production retreated 1.1% in the quarter ended in June, over the quarter ended in March, reflecting retraction of 1.4% in the manufacturing industry, while mining increased 2%. The quarterly evolution was influenced by the retraction in the industries of medical-hospital instrumentation equipment (14.6%); electronic material and communication equipment (7.1%); food (6.1%) and pharmaceutical products (5.4%), offset by the expansion of 8.7% in the motor vehicle industry in the reporting period. Considering observed data, industrial production decreased 5.5% in the month, year-over-year, 3.8% in the year and 2.3% in twelve months, mainly reflecting the unfavorable performance of the capital goods and durable consumer goods industries.



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53. The Nuci in the manufacturing industry reached 84% in August, a 0.3 p.p. increase month-on-month, according to data seasonally adjusted by the FGV. The monthly result stemmed from the expansions of 4.3 p.p. in durable consumer goods, 1.6 p.p. in capital goods, and 0.2 p.p. in intermediate goods, while non-durable consumer goods and construction inputs decreased 0.4 p.p. Considering the observed series, the Nuci increased 0.4 p.p., year-over-year, as a result of the increase in non-durable consumer goods (3.6 p.p.) and durable consumer goods (2 p.p.), as opposed to the decrease in the indicators related to construction inputs (-1.6 p.p.), capital goods (-1.2 p.p.) and intermediate goods (-0.3 p.p.).
54. Vehicles output reached 297.8 thousand units in July, representing increases of 2.8% month-on-month and 0.3% in the quarter ended in July, according to data released by the National Association of Automotive Vehicle Manufacturers (Anfavea), seasonally adjusted by the BCB. Considering observed data, there were retreats of 3.6% year-over-year, 8.3% in the year and 6.5% in twelve months.
55. According to data released by Anfavea, national vehicle licensing decreased 4.6% in July, month-on-month, and increased 20.1% in the quarter, considering data seasonally adjusted by the BCB. Regarding observed data, there were changes of 23.1% year-over-year, 2% in the year and -3.1% in twelve months. Automobile exports totaled 29.7 thousand units in July, representing retractions of 36.1% year-over-year, 14.9% in the year and 3.9% in twelve months. According to the series seasonally adjusted by the BCB, exports decreased 10.6% in the month and 28.6% in the quarter.
56. The LSPA survey carried out by the IBGE regarding July projected 163.3 million tons for the 2012 national harvest of grains, representing increases of 2% year-over-year and 1.6% over the June crop forecast. The new prognosis presented more favorable prospect for the harvest of corn, with increase of 3.5% month-on-month, in contrast to the forecasts for the crops of beans and rice, which reduced by 0.7% and 0.1%, respectively, according to the same comparison basis. Regarding the 2011 harvest of grains, the new projection estimates expansion in the harvest of corn (27%), exclusively reflecting an expected increase of 71.8% for the second harvest, as opposed to the declines projected for the harvests of beans (-18.1%), rice (-14.9%), soybeans (-12.2%) and wheat (-7.9%). In addition, a decrease of 7.6% is projected for the harvest of sugarcane, year-over-year, 0.2% below the previous estimate.

Surveys and Expectations

57. The Consumer Confidence Index (ICC), considering data seasonally adjusted from the nationwide Consumer Expectations Survey (FGV), decreased 1% in August, month-on-month, to 120.4 points, driven by the reduction of 1.4% in the Current Situation Index (ISA) and the expansion of 0.3% in the Expectations Index (IE). The ICC increased 1.4% year-over-year, considering observed data, as a result of the increase of 5.3% in the IE and retreat of 3.9% in the ISA.
58. The ICS, calculated by the Services Survey carried out by the FGV, decreased 2.6% in August, month-on-month seasonally adjusted, moving from 120.6 to 117.5 points, as a result of the decreases of 2.2% in the Current Situation Index (ISA-S) and 2.9% in the Expectations Index (IE-S).
59. The Commerce Confidence Index (ICOM), measured by the Commerce Survey from the FGV, reached 124 points in July, decreasing 4.3% year-over-year. The result reflected reductions of 0.6% in the Current Situation Index (ISA-COM) and 6.4% in the Expectations Index (IE-COM). In the quarter ended in July, the ICOM decreased 3.4% year-over-year, due to the retreats of 2.3% in the ISA-COM and 4.2% in the IE-COM.
60. The Industry Confidence Index (ICI), considering seasonally adjusted data from the Survey of Manufacturing Industry (SCIT-FGV), increased 1.4% in August, month-on-month, reaching 104.1 points. The result was driven by the increase of 2.4% in the ISA and 0.3% in the IE. The ICI increased 1.4% in August, year-over-year, due to increases of 1.3% in the ISA and 1.4% in the IE.
61. The Construction Confidence Index (ICST), measured by the Construction Survey, from the FGV, reached 121.4 points in July, decreasing 10.5% year-over-year. The result reflected retreats of 11.4% in the Current



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Situation Index (ISA-ICST) and 9.7% in the Expectations Index (IE-ICST). In the quarter ended in July, the ICST decreased 9.9%, year-over-year, due to the retreats of 10.6% in the ISA-ICST and 9.2% in the IE-ICST.

Labor Market

62. According to the General Record of Employment and Unemployment (Caged) of the Ministry of Labor and Employment (MTE), 142.5 thousand formal jobs were created in July, of which 39.1 thousand jobs were created in the services sector, 25.4 thousand jobs in the civil construction, 24.7 thousand jobs in the manufacturing industry, 24 thousand jobs in agriculture and livestock sector, and 22.8 thousand jobs in commerce. In the year through July, 1 million thousand jobs were created and in twelve months, 1.2 million, compared to 1.4 million and 1.9 million, respectively, in the same periods of 2011. Month-on-month, formal job creation expanded by 0.3%, considering data seasonally adjusted by the BCB.
63. In July, there was no disclosure of the IBGE employment survey (PME) data for the metropolitan regions of Rio de Janeiro and Salvador, and consequently, to the total of the areas covered by the survey. The unemployment rate decreased, in July, in three of the four metropolitan regions with data released, especially in São Paulo, which reached 5.7%, with a decrease of 0.8 p.p. in July, month-on-month, and equal change compared to the same month of the previous year. The monthly result was driven by retraction of 0.7% in the Economically Active Population (PEA) while the Employed Population (PO) increased by 0.1%. In the metropolitan region of Belo Horizonte, the unemployment rate reached 4.4% in July, a decrease of 0.1 p.p. compared to previous month and 0.3 p.p. compared to July 2011. This monthly change was due to the slight reduction of the PEA and the stability in the OP. The unemployment rate in the metropolitan region of Porto Alegre decreased 0.2 p.p. in July, month-on-month, reaching 3.8%, influenced by a fall of 3% in the PEA, greater than the 2.8% retreat observed in the PO. Compared to July 2011, the rate decreased 0.9 p.p. Out of the four metropolitan regions with data released by the IBGE, the unemployment rate increased only in the metropolitan region of Recife, 6.5%, compared to 6.3% in June, due to a decrease of 1.3% in the PO, while the PEA recorded a fall of 1.2%. Compared to July 2011, the rate also increased 0.2 p.p.. According to the same survey, the average real income usually received in the metropolitan region of Porto Alegre grew 0.2% in July, month-on-month, and 0.7%, year-over-year. Recife, Belo Horizonte and São Paulo recorded retractions in the monthly comparison, of 3.5%, 1.8% and 1.1% respectively. Year-over-year, there was expansion in the metropolitan regions of Belo Horizonte, 5.2%; Recife, 5.1%; and São Paulo, 1.8%. Month-on-month, real payroll, defined as the product of the number of persons employed by the usual real average income of the main work, declined in the four metropolitan regions: Porto Alegre, 0.5%; Belo Horizonte, 0.4%; São Paulo, 0.3%; and Recife, 0.3%. Year-over-year, there were expansions of 0.1%, 7.1%, 4.1% and 15.5%, in this order.

Credit and Delinquency Rates

64. Outstanding credit in the financial system reached R\$2,167 billion in June, equivalent to 50.6% of GDP, increasing by 1.5% in the month, 6.8% in the year and 17.9% in twelve months. Non-earmarked credit operations, which represented 64.1% of the total of the financial system, increased 1.4% in the month, 6.4% in the year and 15.7% in twelve months, reflecting respective increases of 0.9%, 5.7% and 14.4% for credit operations to individuals, and 1.8%, 7.2% and 17.1% for credit operations to corporate, in the same order. Earmarked credit operations increased 1.7% in the month, 7.4% in the year and 21.8% in twelve months. It bears highlighting the expansions of 2.8%, 17% and 39% in housing credit, according to the same comparison bases.
65. The average annual interest rate on reference credit operations reached 31.1% p.y. in June, decreasing 1.8 p.p. in the month and 8.4 p.p. in twelve months. The average annual rate on credit for individuals and corporate reached 36.5% p.y. and 23.8% p.y., respectively, registering respective decreases of 2.3 p.p. and 1.2 p.p., month-on-month, and 9.6 p.p. and 7 p.p., year-over-year.
66. The average tenure on reference credit operations increased three days in June, reaching 503 days. The tenure related to individuals and corporate segments increased three and five days, reaching 610 and 406 days, respectively.



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67. The delinquency rate in the financial system (non-earmarked loans used as reference for interest rates, in arrears for more than ninety days) reached 5.8% in June, decreasing 0.1 p.p. month-on-month and increasing 0.7 p.p. year-over-year. The indicator for the operations with individuals reached 7.8% in May, decreasing 0.1 p.p. month-on-month, and increasing 1.4 p.p. in twelve months. The delinquency rate for credit operations to the corporate segment reached 4%, retracting 0.1 p.p. on a month-on-month basis and increasing 0.2 p.p. year-over-year.

External Environment

68. The release of the GDPQ2 figures in the main economies confirmed the prospects for economic deceleration. In the US, the quarterly GDP change decelerated to 1.5%, annualized, down from 2% in the first quarter, mainly reflecting deceleration in the consumption personal expenses and in the fixed capital gross formation, as well as more accelerated growth of imports of goods and services compared to exports. In the Euro Area, economic activity contracted 0.7%, in annualized terms, after expanding by 0.1% in the previous quarter, with German growth decelerating to 1.1%, down from 2% in the previous quarter. The UK recorded contraction for the third consecutive quarter, -1.8%, compared to -1.3% in the first quarter. In Japan, GDP grew at an annualized rate of 1.4%, compared to 5.5% in the first quarter. China, conversely, expanded 7.4% on a quarterly basis, up from 6.6%, according to the same comparison bases, considering annualized rates.
69. In the US, July indicators for industrial production, retail sales, consumer confidence (*Conference Board*) and jobs creation breached the respective averages recorded in the quarter ended in June. Housing market conditions suggest some improvement in the recent months, although the activity in this sector remains at low levels. In the Euro Area, the unemployment rate in June, 11.2%, reached the record high for the series, reflecting in the deterioration in the economic sentiment and consumer confidence indices. The first recorded, in July, the record low since October 2009, while the second one reached, in August, the worst result since July 2009. The regional composite PMI advanced indicator, released by *Markit Economics*, reached 46.6 in August, indicating contraction for the seventh consecutive month. In China, the industrial production in July increased relative to the average recorded in the second quarter, while the retail sales remained stable and the investments in fixed assets reduced, according to the same comparison bases.
70. In the financial markets, several indicators reported reduction in the risk perception, despite the maintenance of the uncertainties regarding the evolution of the crisis in some European economies and the recovery of economic activity in the main global economies. The CBOE VIX index reduced to a level observed previous to the Lehman Brothers bankruptcy, the main stocks markets valued, the US dollar retreated against the main currencies, the composite Embi⁺ declined, and the ten-year interest rates of the US and Germany sovereign securities increased.
71. Among international commodities prices, it bears highlighting the increases in the prices of corn, soybeans, wheat and oil, the first three of which reflecting strong droughts in producer regions of the US and Russia, while the prices of oil suffer the impact, among other factors, of the economic embargo to Iran, of the maintenance of platforms in the North Sea and of the reduction in the US inventories. Conversely, the prices of sugar, coffee and iron ore registered significant lows since the last Copom meeting.
72. Since the last Copom meeting, the process of global disinflation has continued, with the maintenance of the declining trend of the consumer price indices (IPC) annual change in advanced economies, for which contributed, in twelve months, the reduction in energy prices. The IPC annual change reached 1.4%, 2.4% and 2.6%, in the US, Euro Area and United Kingdom, respectively, in July, and -0.1% in Japan, in June. In developing economies, it bears highlighting the retreat in annual consumer inflation in China to 1.8% in July. Under this scenario, the monetary policy interest rates in developed economies were maintained since the last Copom meeting. In the other economies, the rates were also maintained at the levels valid previously to the Copom meeting, except for South Korea, Philippines, Colombia, South Africa and Hungary, whose central banks chose for reductions in the respective basic interest rates.

Foreign Trade and International Reserves



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73. The Brazilian trade surplus reached US\$2.9 billion in July, as a result of US\$21 billion in exports and US\$18.1 billion in imports. In the year through July, the trade surplus totaled US\$9.9 billion, down from US\$16.1 billion in the same period of 2011, reflecting retreat of 3% in exports and expansion of 1.7% in imports, according to the daily average criterion. In the year through July, total external trade declined 0.8%, according to the daily average criterion, totaling US\$266.5 billion in the year.
74. International reserves reached US\$376.2 billion in July, increasing US\$2.2 billion month-on-month. Compared to December 2011, the reserves increased US\$24.1 billion. In the month, there were no monetary authority's interventions in the domestic spot market.

Money Market and Open Market Operations

75. After the July Copom meeting, the domestic interest rate yield curve increased its slope, with retreat in the short-term rates and increase in the rates above one year. The movement in the short part of the curve reflected, mainly, the prospect of continuity in the fall of the Selic rate and the uncertainties related to the pace of recovery in domestic economic activity. In the long part, the increase in the rates was influenced, at the domestic scenario, by the release of several current inflation indices above the expected and by the increase of inflation expectations. At the external scenario, the increase in the prices of agricultural commodities and the expectation of announcement of the new monetary stimuli measures by the Fed also contributed for the elevation of the long-term rates. Between July 6th and August 27th, the one-, three- and six-month interest rates fell by 0.50 p.p., 0.42 p.p. and 0.27 p.p., respectively. The rates for maturities of one, two and three years increased by 0.06 p.p., 0.23 p.p. and 0.07 p.p., respectively. The real interest rate, as measured by the ratio between the nominal rate of one year and expected inflation (smoothed) for the next twelve months, slightly decreased from 1.85% on July 6th, to 1.78% on August 27th, mainly due to the increase in the IPCA projection.
76. On August 21st, the BCB carried out reverse FX swap auctions maturing on September 3rd, totaling the equivalent to US\$350 million. The net result of swap BCB operations is US\$5.9 billion, borrowing in FX change.
77. In its open market operations, the BCB carried out weekly, between July 10th and August 27th, repo operations borrowing R\$52 billion for a six-month period. The average daily balance of the long term operations increased from R\$127.8 billion, between May 29th and July 9th, to R\$131.8 billion, between July 10th and August 27th. In the same period, the BCB also borrowed money through very short term repo operations with tenures between thirteen and thirty-five working days, increasing the average daily balance of short-term borrowing operations to R\$353.5 billion. The BCB also conducted very short-term operations through 36 borrowing operations, and carried out leveling operations, at the end of the day, with tenures of one and two working days. The average daily balance of these operations totaled R\$82.3 billion in the period, borrowing. The average daily balance of the total outstanding of repurchase agreements of the BCB increased from R\$468.3 billion, between May 29th and July 9th, to R\$567.5 billion, between July 10th and August 27th. Considering the operations for the most recent period, the total outstanding of repurchase agreements decreased from R\$578.6 billion on July 9th to R\$567.4 billion on August 27th. The main factor that contributed to the retraction of liquidity in the period was the net revenue of the Union.
78. Between July 10th and August 27th, the National Treasury issuance regarding the traditional auctions raised a total of R\$42.0 billion. The sale of fixed-rate securities reached R\$33.0 billion, with R\$29.9 billion via issuance of LTNs maturing in 2013, 2014 and 2016, and R\$3.1 billion via NTN-Fs maturing in 2018 and 2023. The sales of inflation-linked NTN-Bs reached R\$9.0 billion, for securities maturing in 2016, 2018, 2022, 2030, 2040 and 2050.