



BRAZILIAN FEDERATION OF BANKS

Economic and financial scenario Brazil 2017-2018

21st ASUTIL Conference, Rio de Janeiro

June 7, 2017

Murilo Portugal
President

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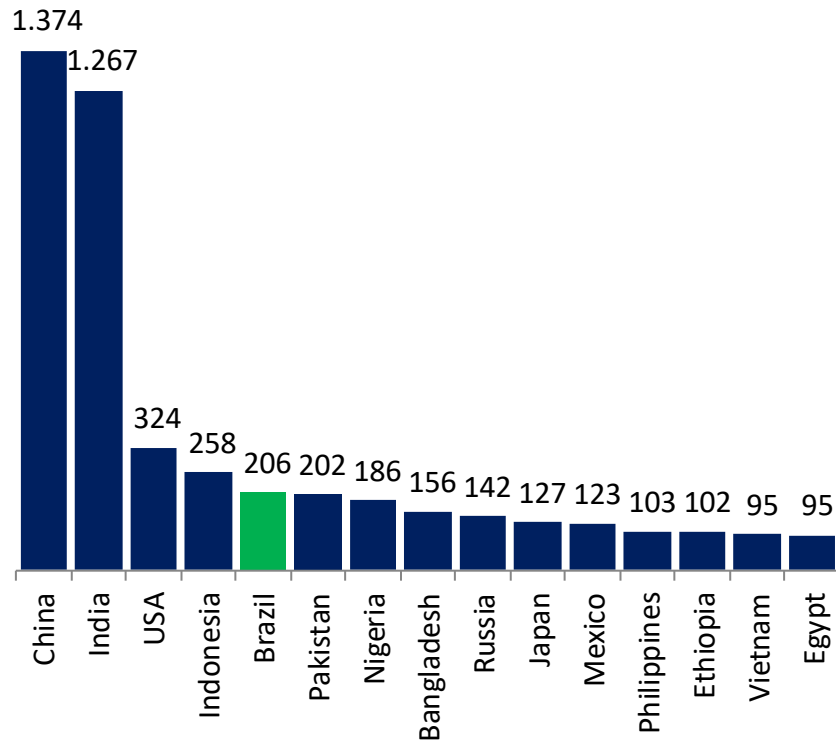
- I. Structural aspects of the Brazilian Economy**
- II. Credit Market and Banking Sector
- III. Recent economic evolution
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General Overview - Populous and large country

5th largest and most populous country in the world

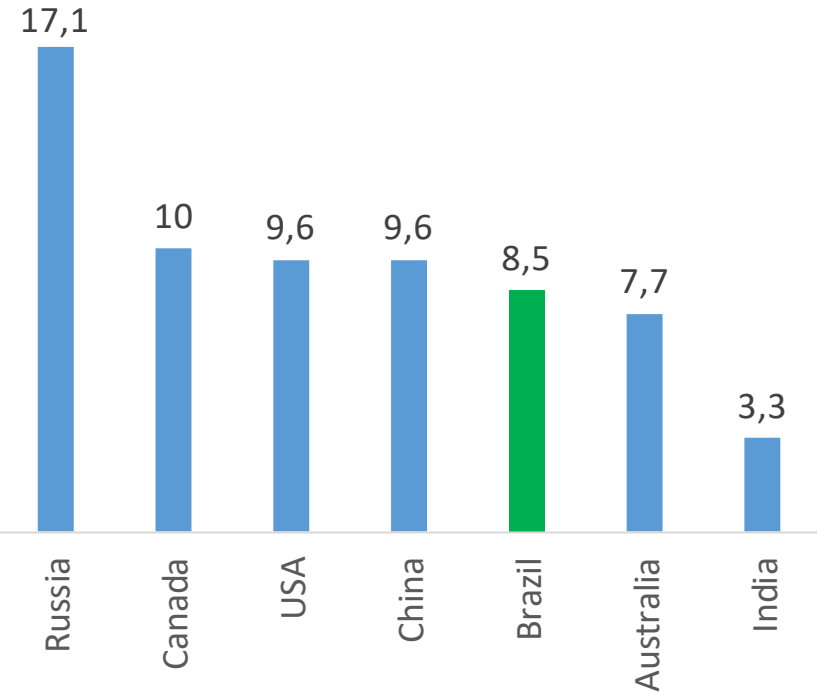
Population

(million inhabitants in 2016)



Territorial Extension

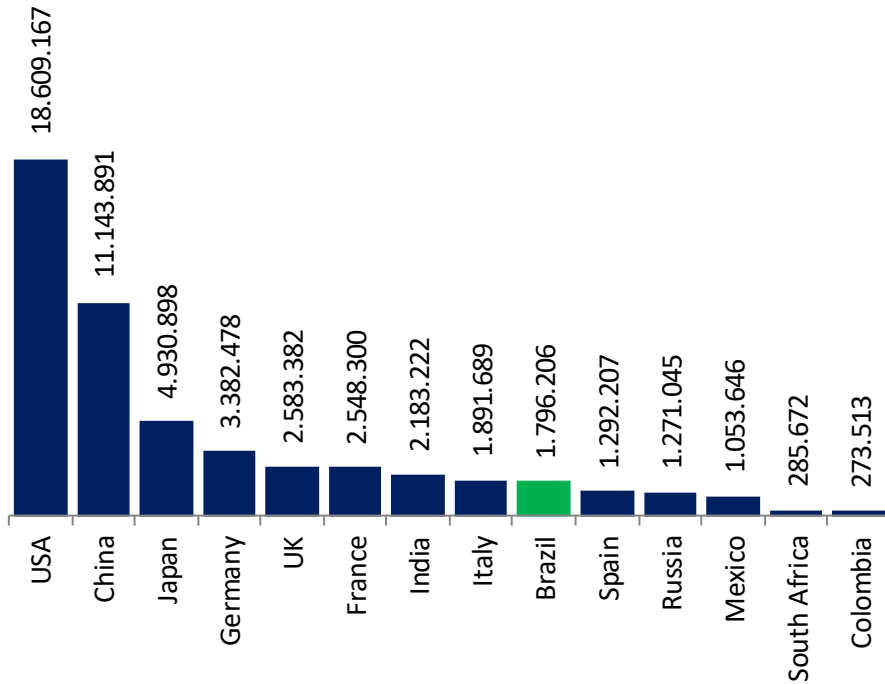
(Km² million)



General Overview: Large middle-income economy

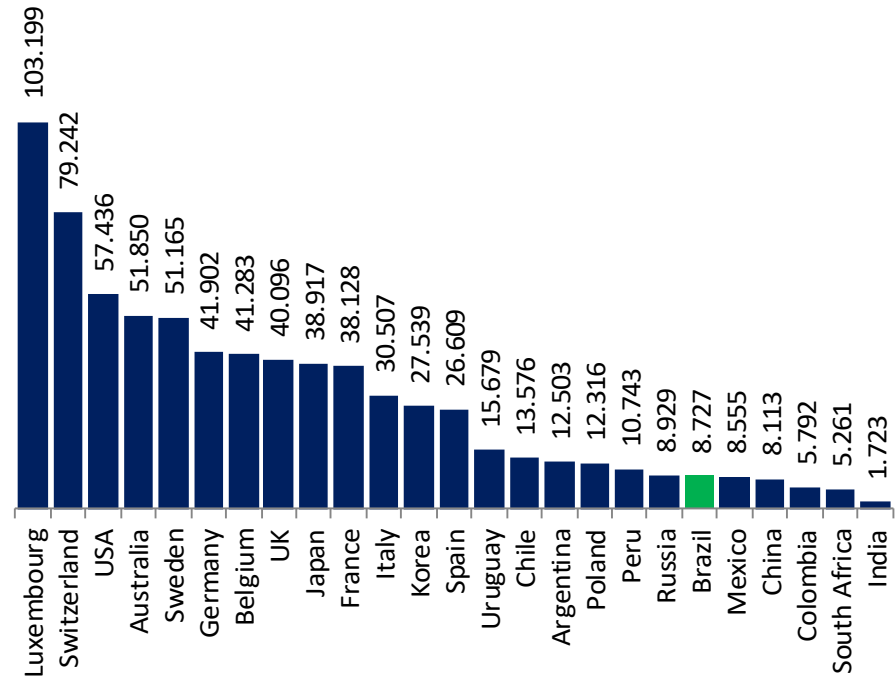
GDP

(US\$ thousand in 2016)



Per capita income

(US\$ thousand in 2016)

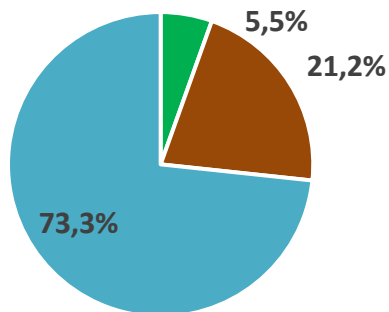


GDP - Supply and Demand

Diversified economy: efficient agriculture and 2nd most diversified industry among emerging markets

GDP

(Supply breakdown in 2016)



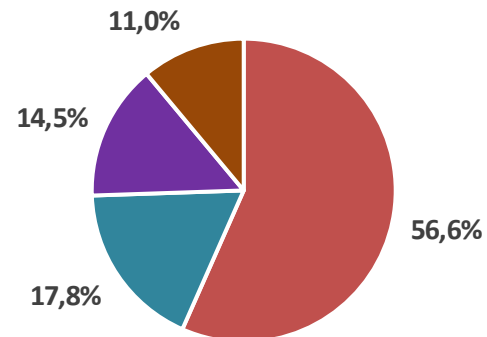
■ Agriculture, Livestock, & Natural Resources ■ Manufacturing ■ Services

% Real Growth



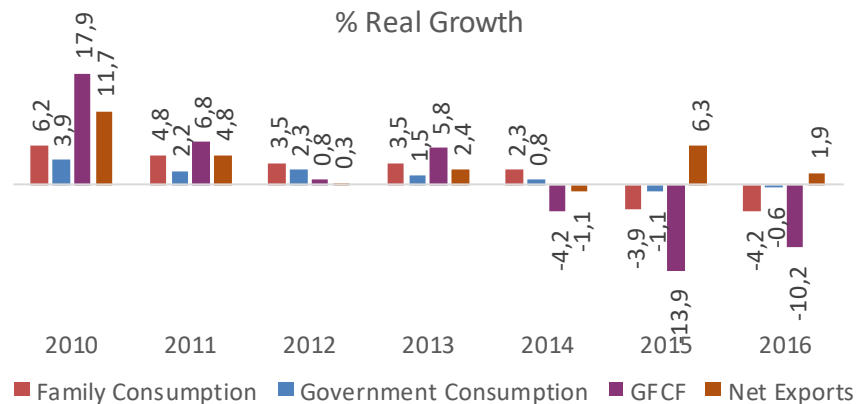
GDP

(Demand breakdown in 2016)



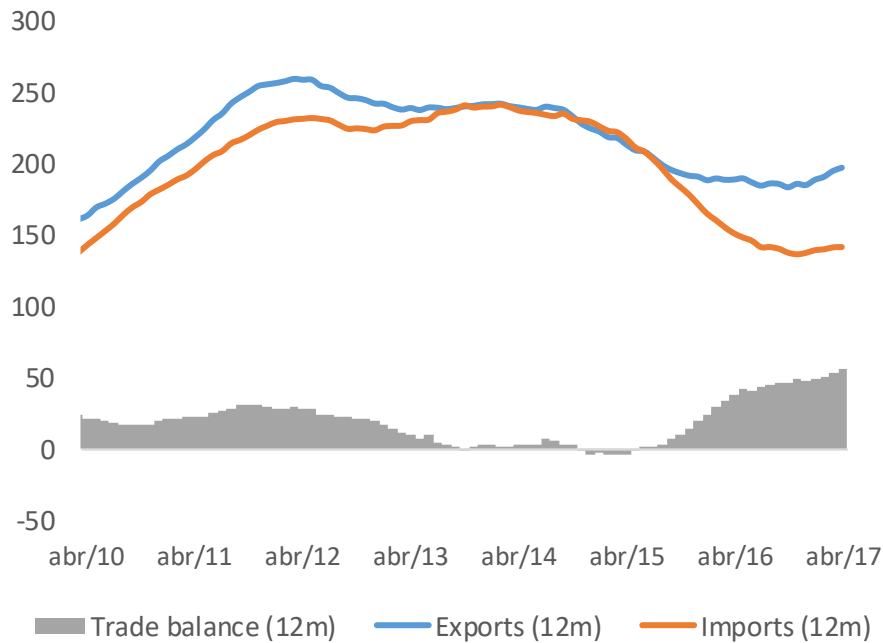
■ Family Consumption ■ Government Consumption
■ Gross Fixed Capital Formation ■ Net Exports

% Real Growth

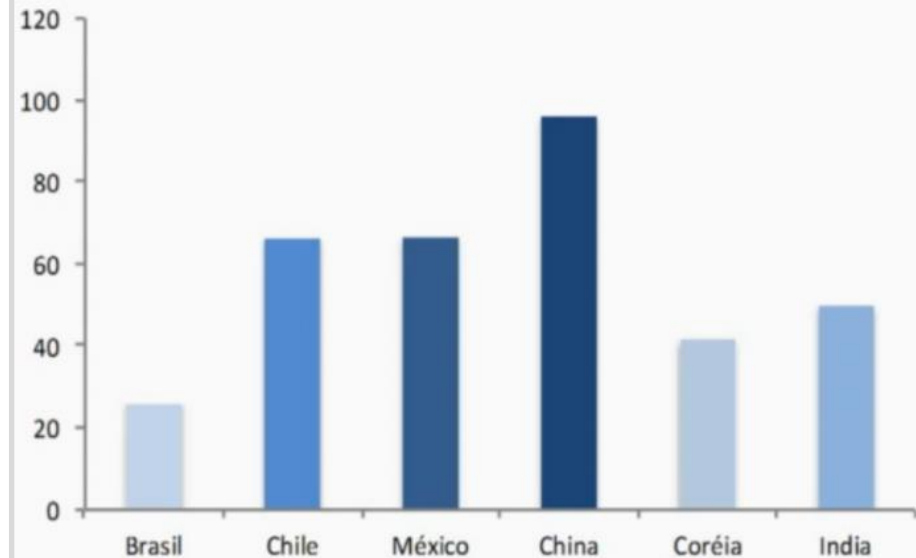


Balance of Trade: recent adjustment and need for greater openness

Balance of Trade (US\$ billions)

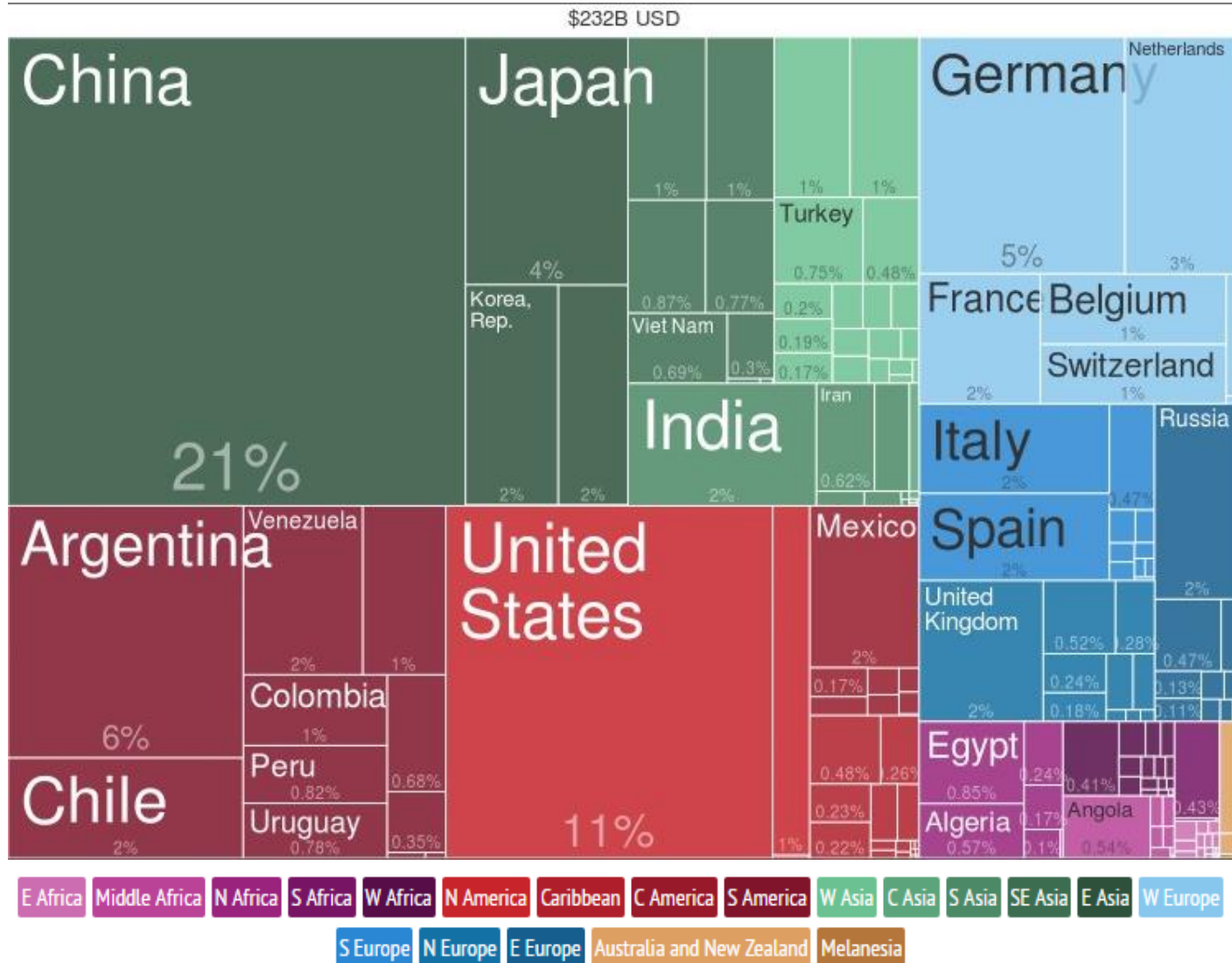


Degree of openness of the economy (Imp. + Exp. / GDP in 2015)



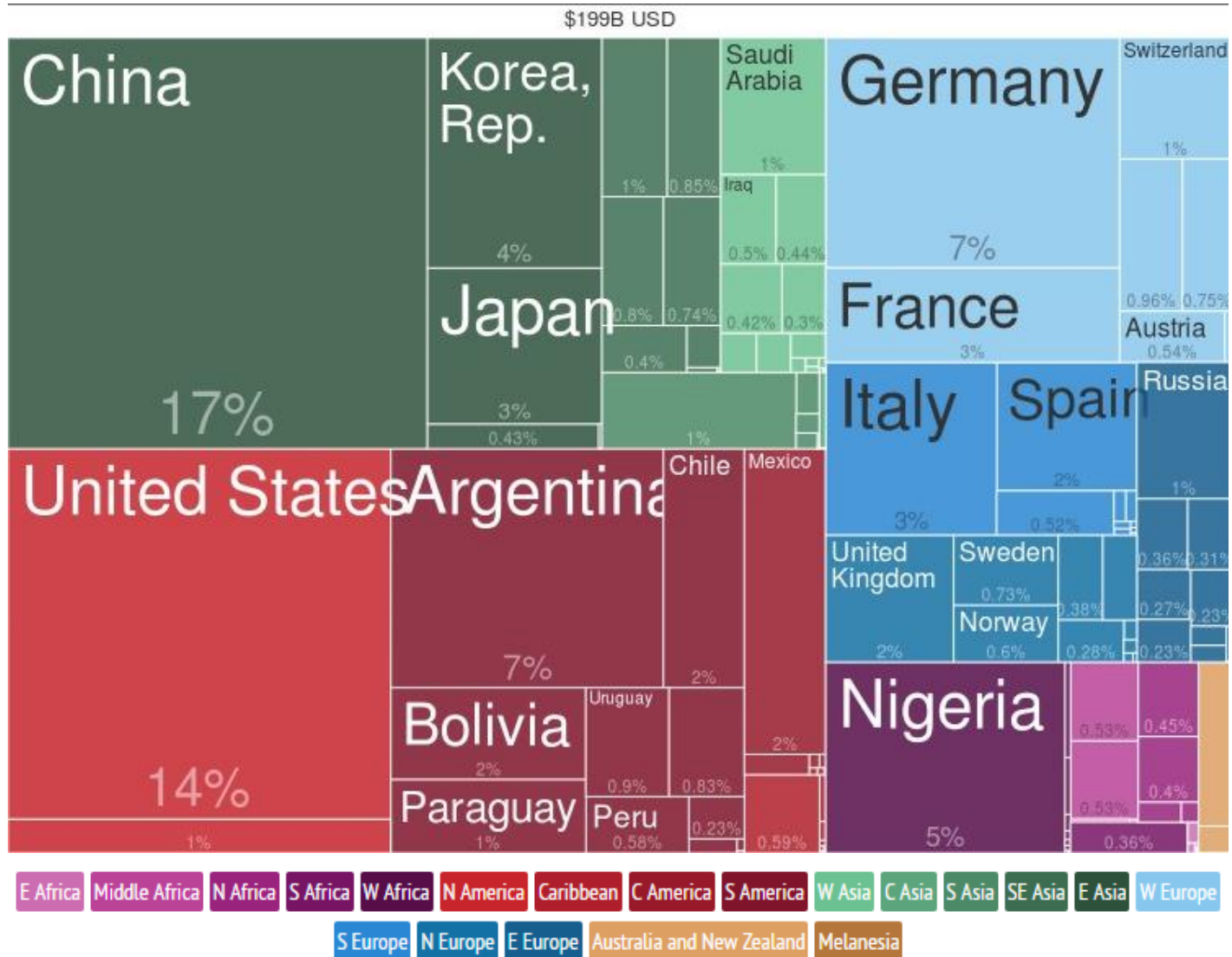
Brazilian Exports: main partners

Geographically diversified exports and imports (2014)



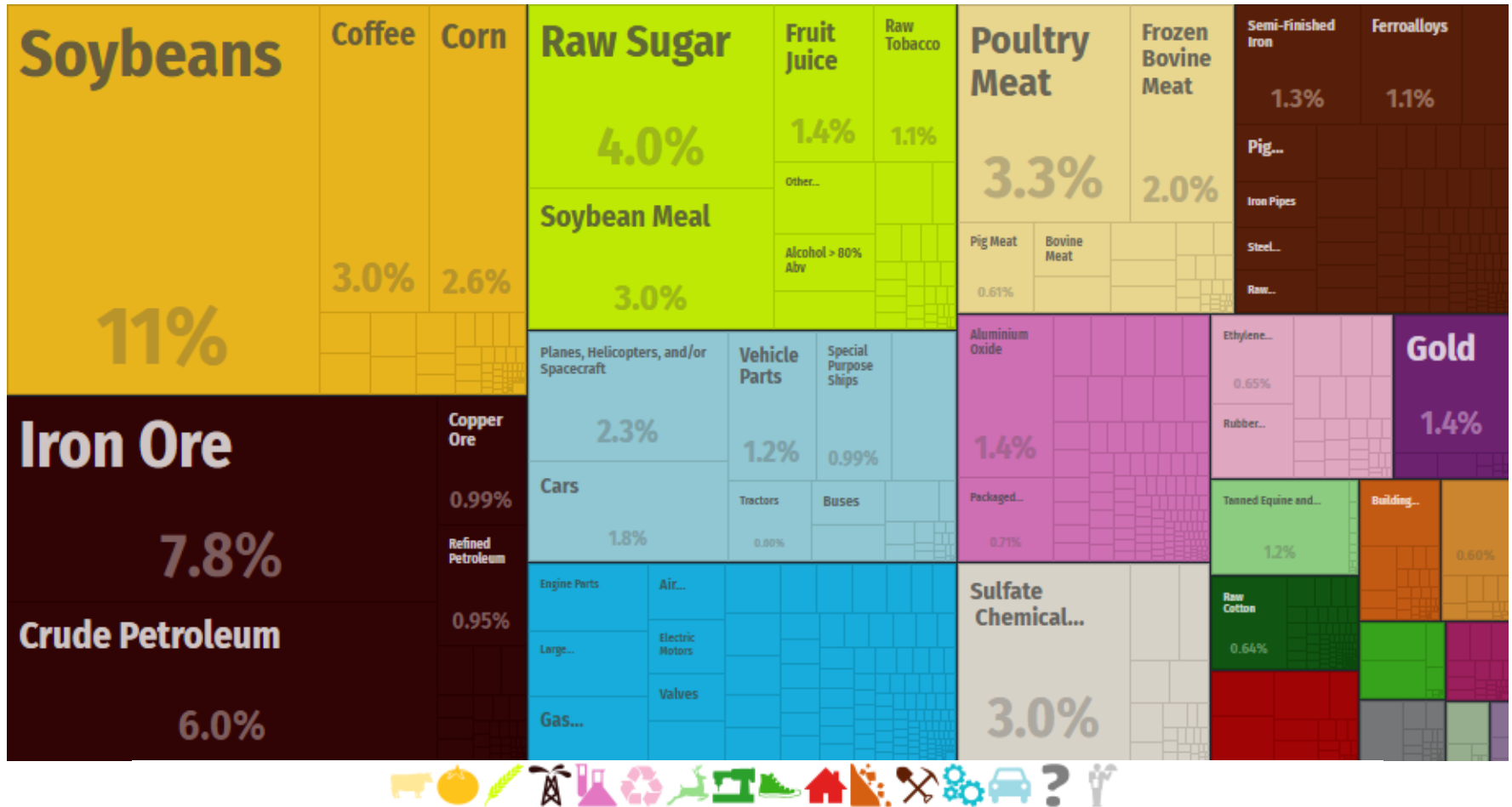
Brazilian Imports: main partners

Geographically diversified exports and imports (2014)



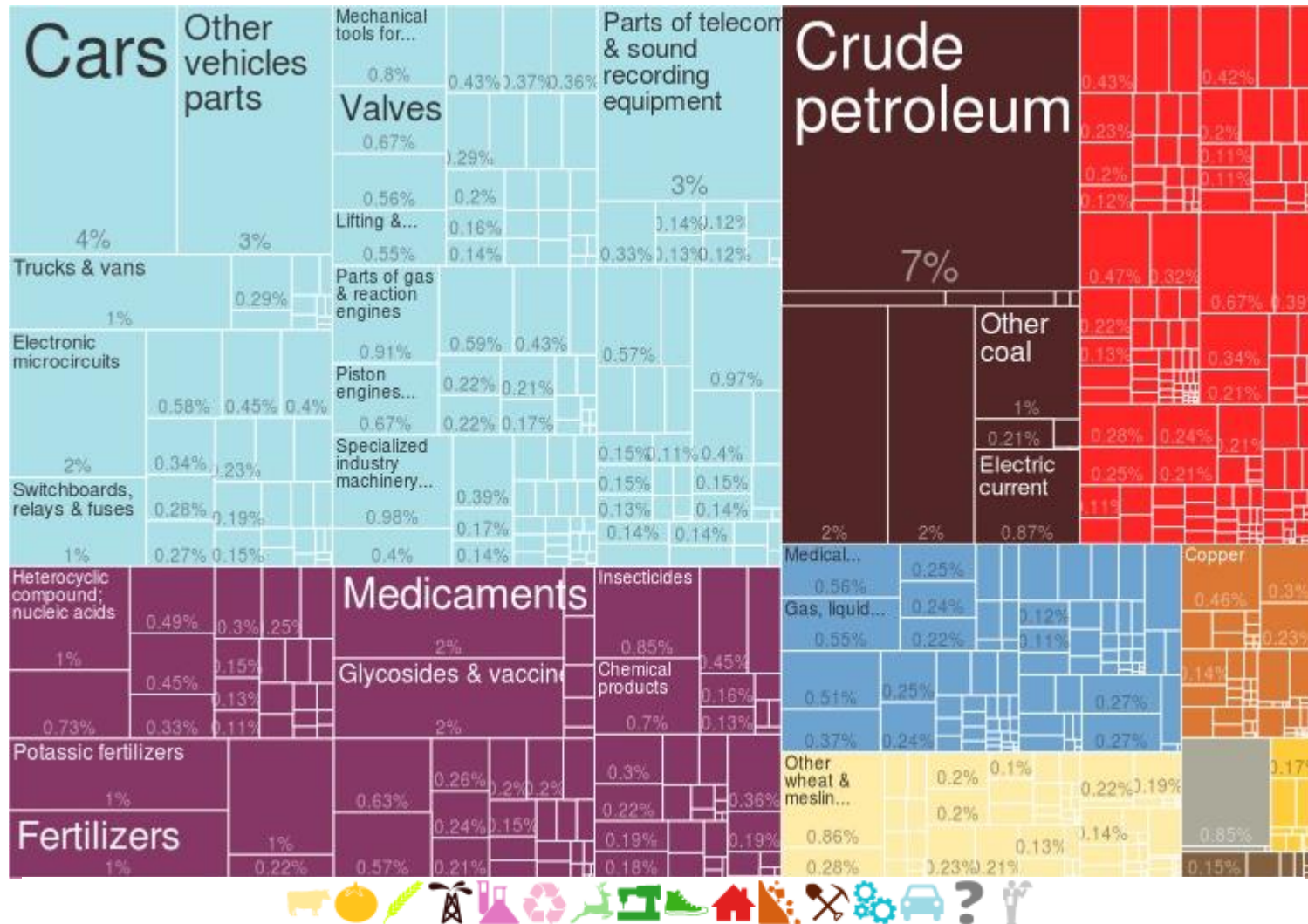
Brazilian Exports: main products

Rich in Natural Resources (2014)



Brazilian Imports: main products

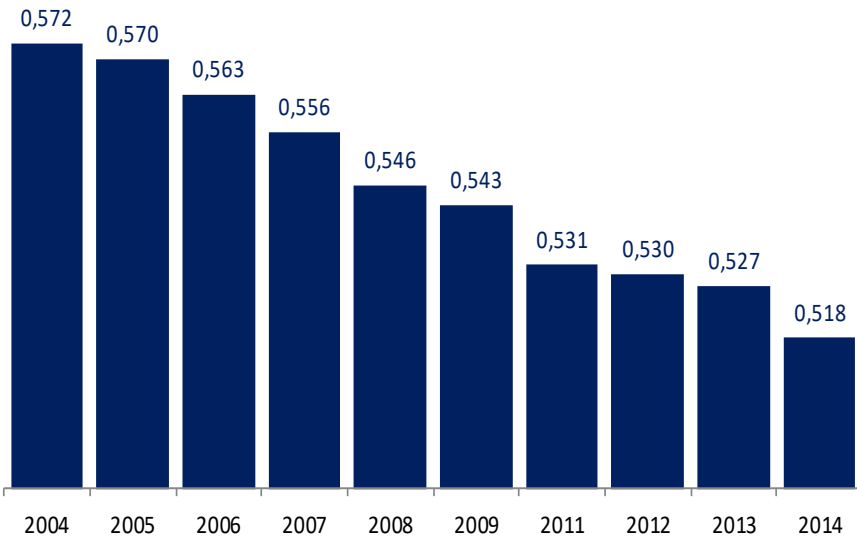
Machinery, Manufactured goods, Chemicals (2014)



Inequality and Poverty

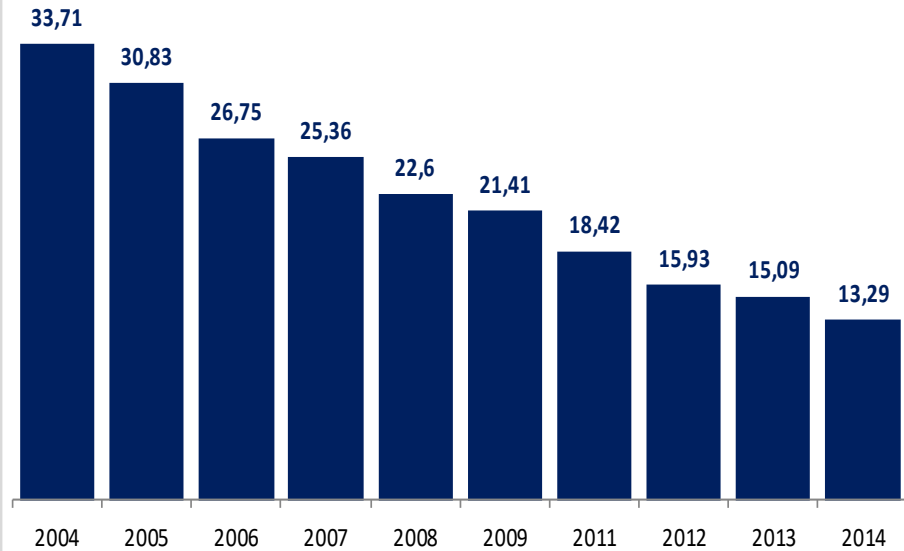
Gini Coefficient

between 0 (perfect equality) and 1 (maximum inequality)



Poverty ratio*

(% of the population)



Source: Pnad-IBGE, IPEA and consultants until 2014 (last data available)

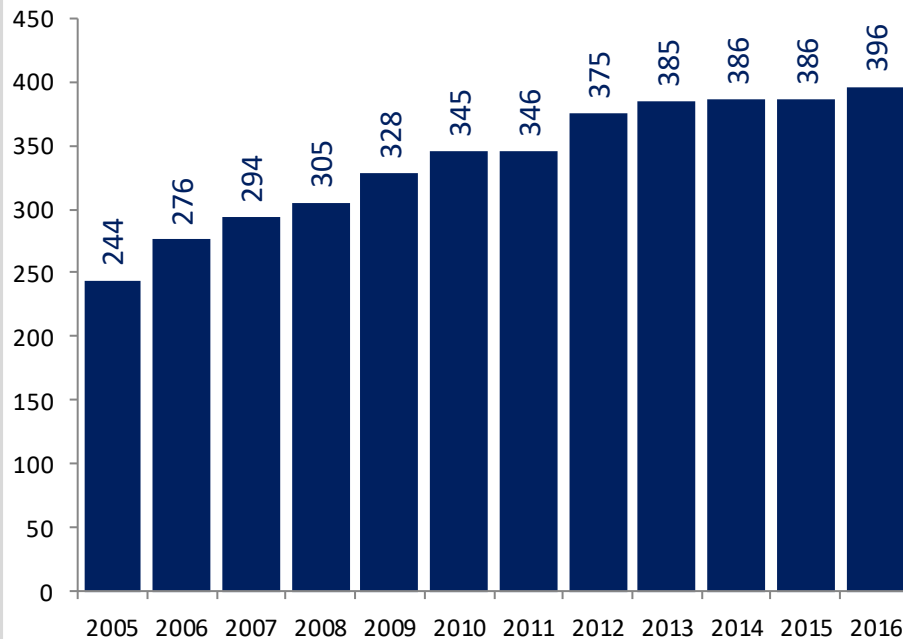
*Poverty (FAO and WHO) defined as insufficient income for a food basket with a minimum of calories (around 2,000 kcal) per individual

Minimum wage and income classes

Increase in the minimum wage and reduction of income inequality

Real minimum wage

(in 2015 constant prices at US\$ PPP)



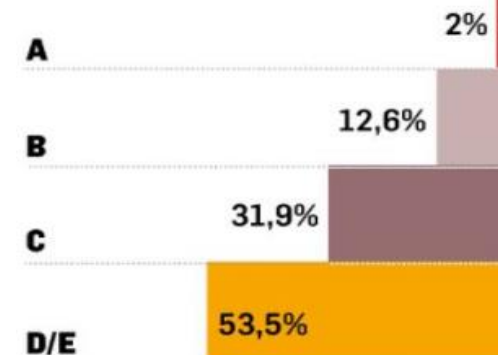
Participation in total income

(% of the income mass and number of families in 2014)

% in total income



% of the number of families



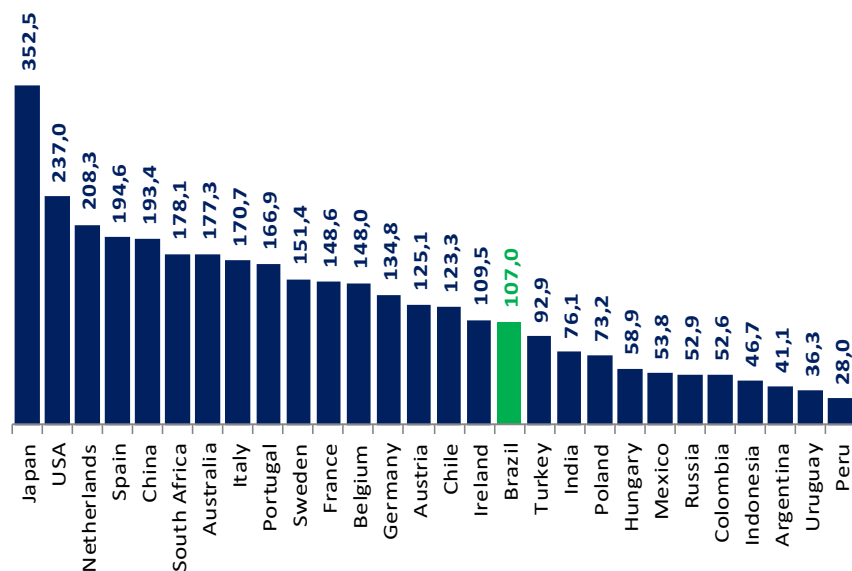
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Total credit and Basel Ratio

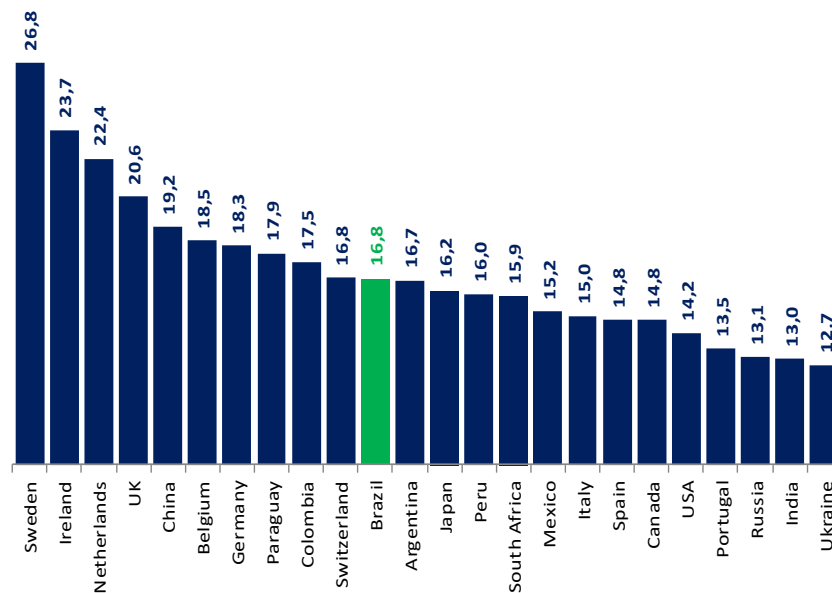
Total Domestic Credit*

(Total Financial Sector % of GDP in 2015)



Basel

Regulatory Capital to Risk Weighted Assets (% in 2016)

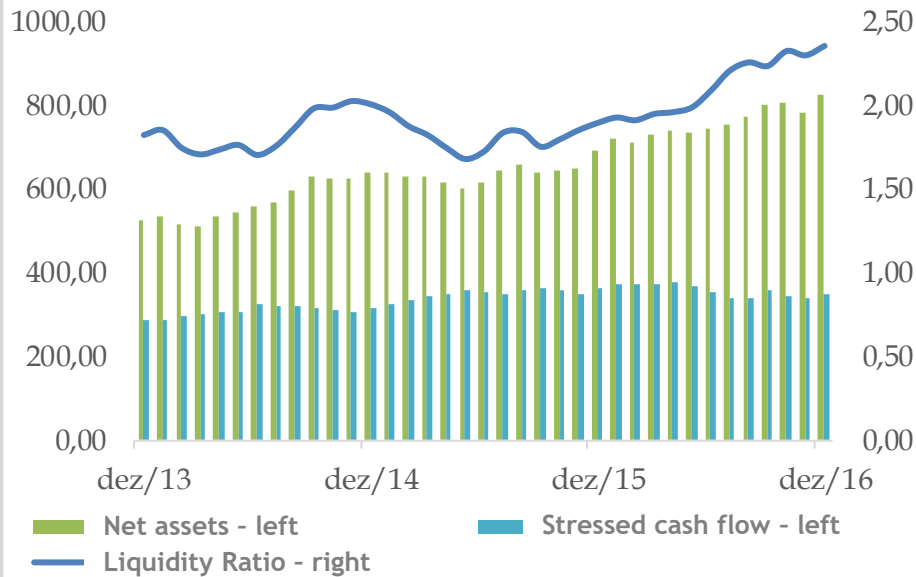


Source: World Bank. *The financial sector includes monetary authorities (the central bank) and deposit money banks, as well as other financial institutions, including institutions that do not accept transferable deposits but do incur such liabilities as time and savings deposits. Examples of other banking institutions are savings and mortgage loan institutions, finance companies, development banks, and building and loan associations.

Banking Sector: comfortable liquidity levels

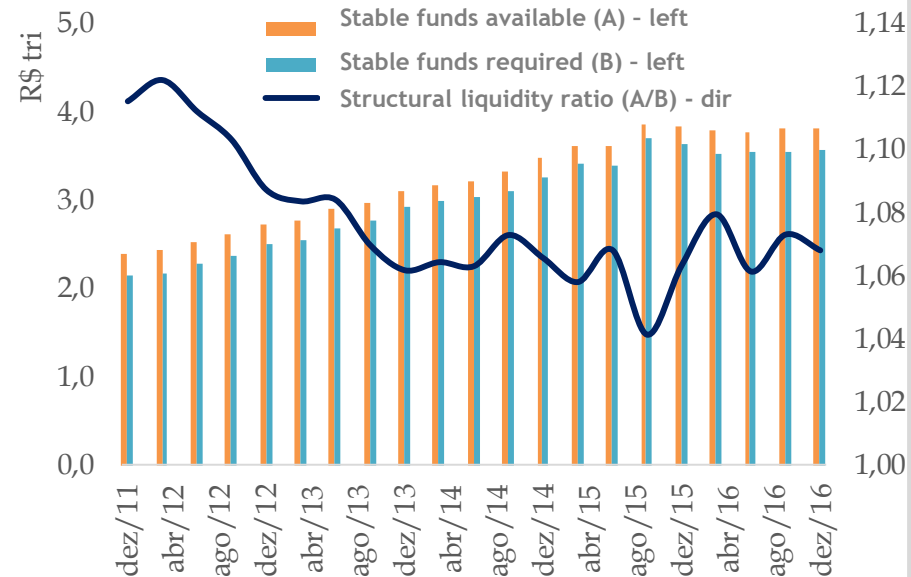
Short-Term Liquidity

(Net Assets / Stressed cash flow)



Long-term Liquidity

(Stable Funds Available / S.F. Required)

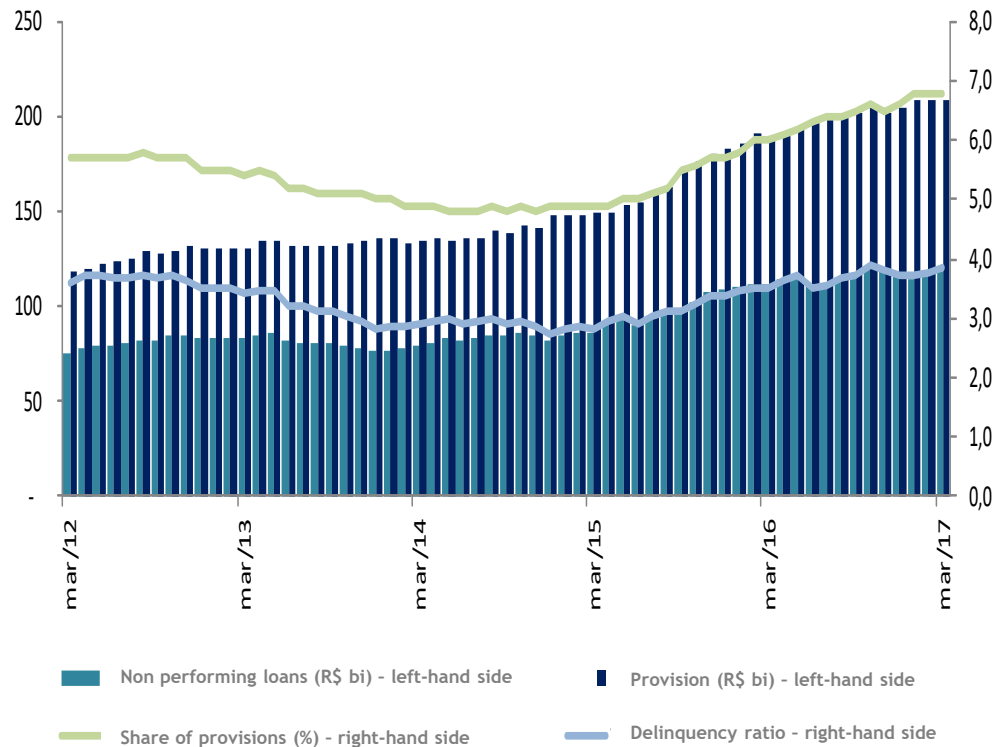


Banking Sector: adequate and secure levels of provisions

Banks hold a high level of provisions against defaults and high-risk transactions

Provisions for NPLs cover 180% of defaults (arrears > 90 days)

Provisions x non performing loans (% of portfolio)



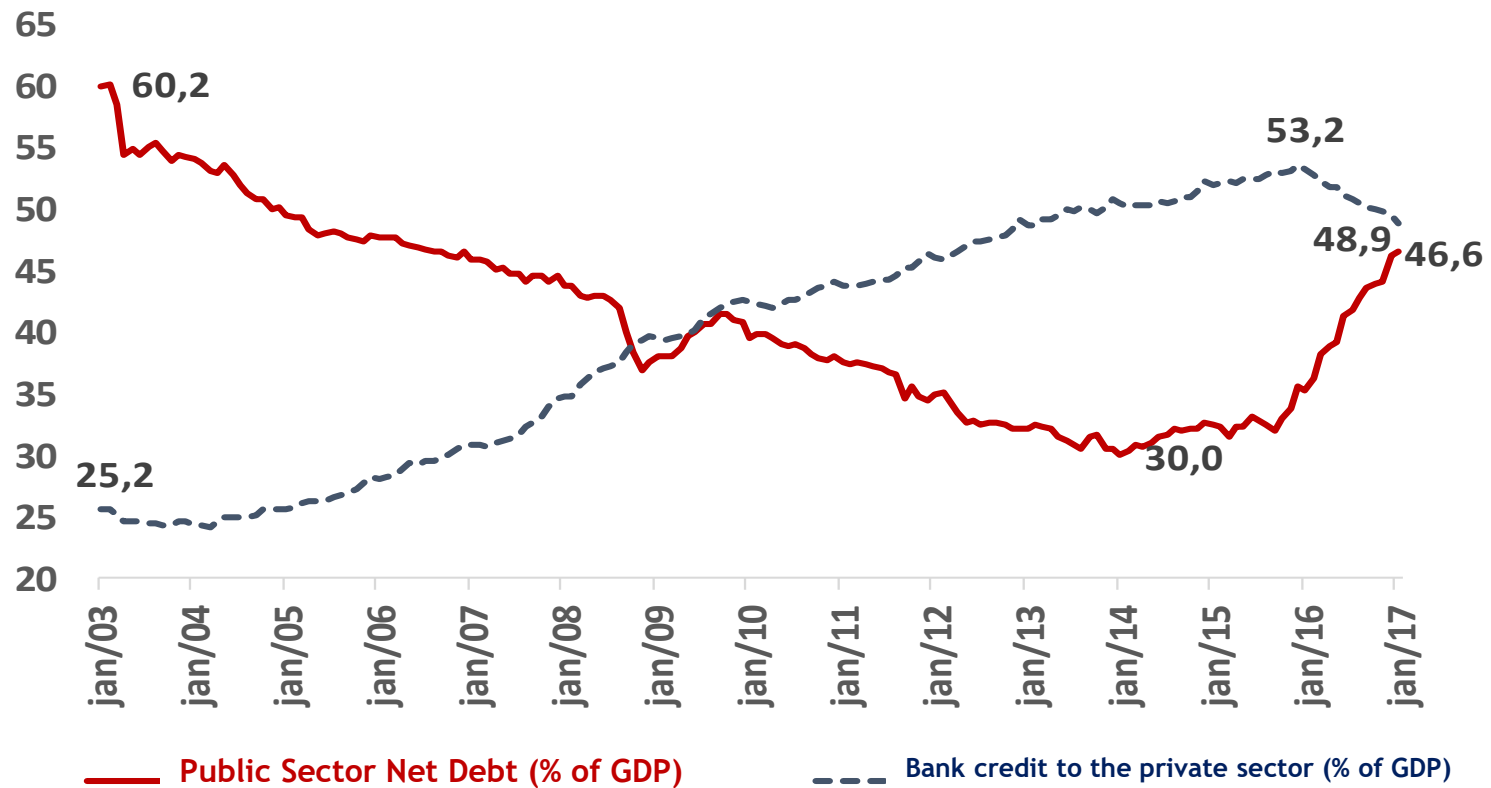
Banking Sector Overview

The 10 largest banks – December 2016

10 Largest Banks	Total Assets (R\$ M)	Total Deposits (R\$ M)	Equity (R\$ M)	Net Profit* (R\$ M)	Basel	ROE	ROA	Number of Branches
BB	1.436.765	447.949	77.040	6.650	18,4	8,6%	0,5%	5.460
ITAU	1.331.841	369.390	129.935	19.486	19,0	15,0%	1,5%	3.494
CAIXA ECONOMICA FEDERAL	1.256.172	513.098	27.180	3.421	13,5	12,6%	0,3%	3.412
BRADESCO	1.081.375	235.821	101.221	13.663	15,4	13,5%	1,3%	5.335
SANTANDER	705.061	146.963	60.009	6.205	16,3	10,3%	0,9%	2.763
SAFRA	148.391	12.589	9.508	1.736	15,4	18,3%	1,2%	114
BTG PACTUAL	131.993	10.894	17.678	2.794	21,5	15,8%	2,1%	13
VOTORANTIM	103.005	4.578	8.426	463	15,0	5,5%	0,4%	95
CITIBANK	72.024	19.374	8.411	1.193	16,5	14,2%	1,7%	134
BANRISUL	68.235	42.783	6.441	540	16,9	8,4%	0,8%	539
Total 10 largest banks	6.334.863	1.803.439	445.849	56.151	17,2	12,6%	0,9%	21.359
Banking System	7.009.784	1.995.174	521.904	62.301	17,1	11,9%	0,9%	22.899
<i>TOP 10 Market Share</i>	<i>90%</i>	<i>90%</i>	<i>85%</i>	<i>90%</i>				<i>93%</i>

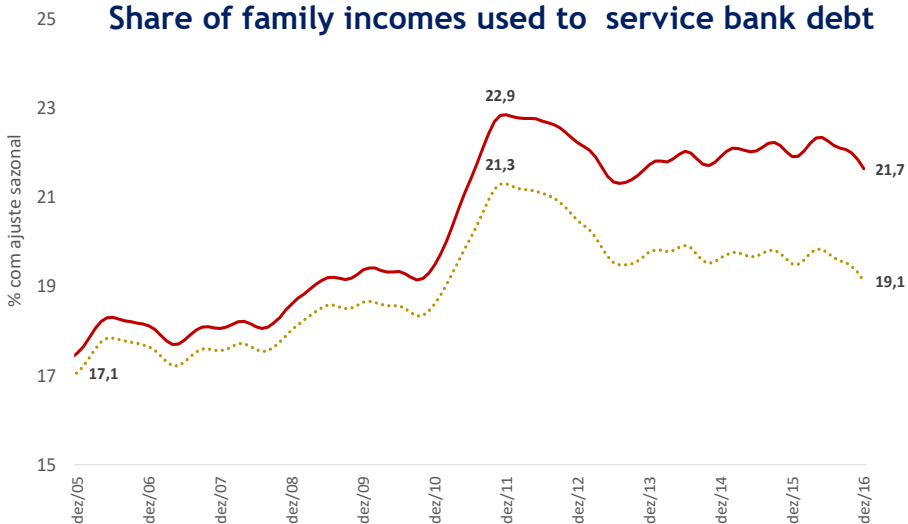
Government indebtedness vs. Bank credit to the private sector

Recent trend towards *Crowding Out* (% PIB)

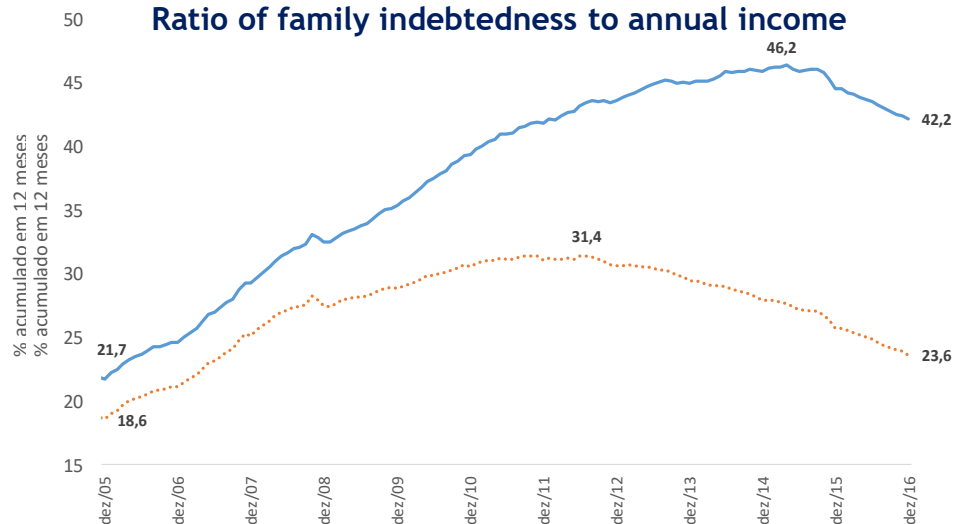


Deleveraging: Families and Business reducing indebtedness

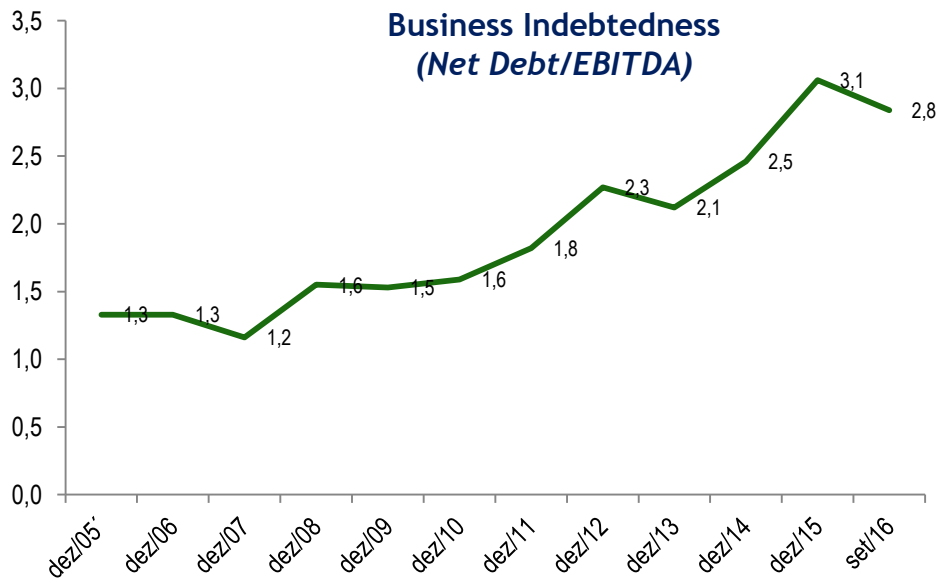
Share of family incomes used to service bank debt



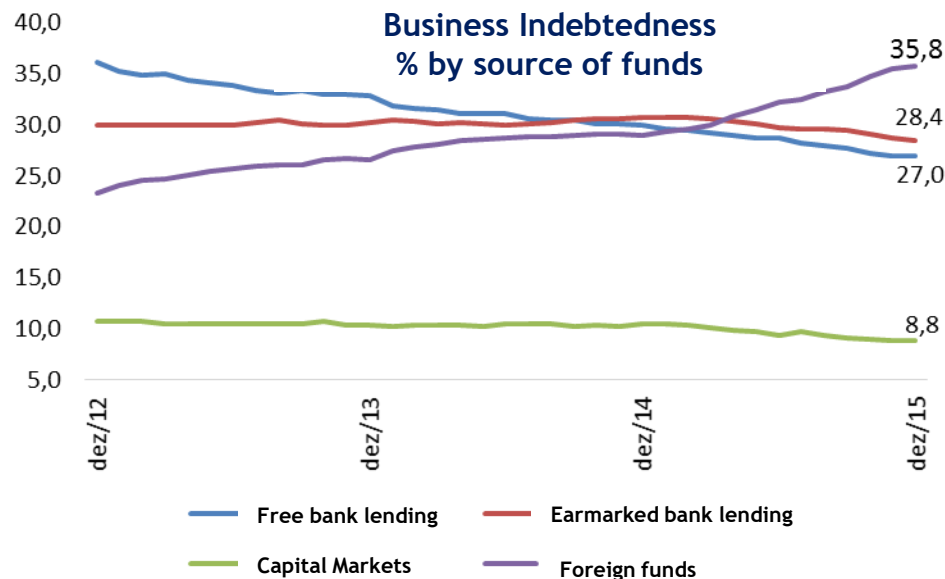
Ratio of family indebtedness to annual income



Business Indebtedness (Net Debt/EBITDA)



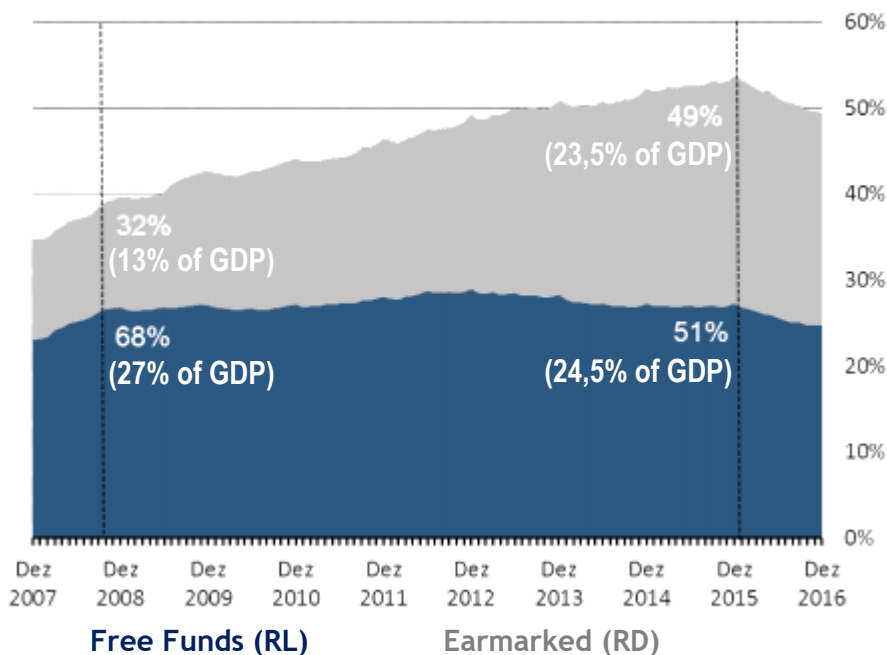
Business Indebtedness % by source of funds



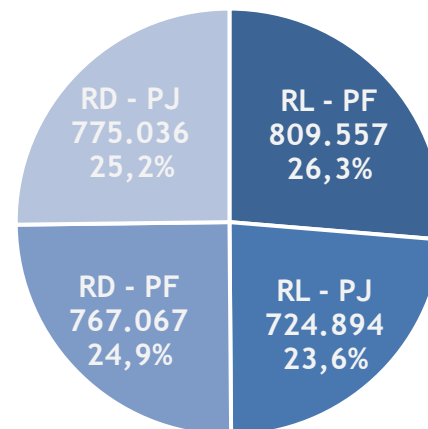
Credit/GDP -Free x Earmarked Funds and Corporate x Consumer Loans (%)

Sources of Funds and allocation of Bank Credit

Credit/GDP By source of funding

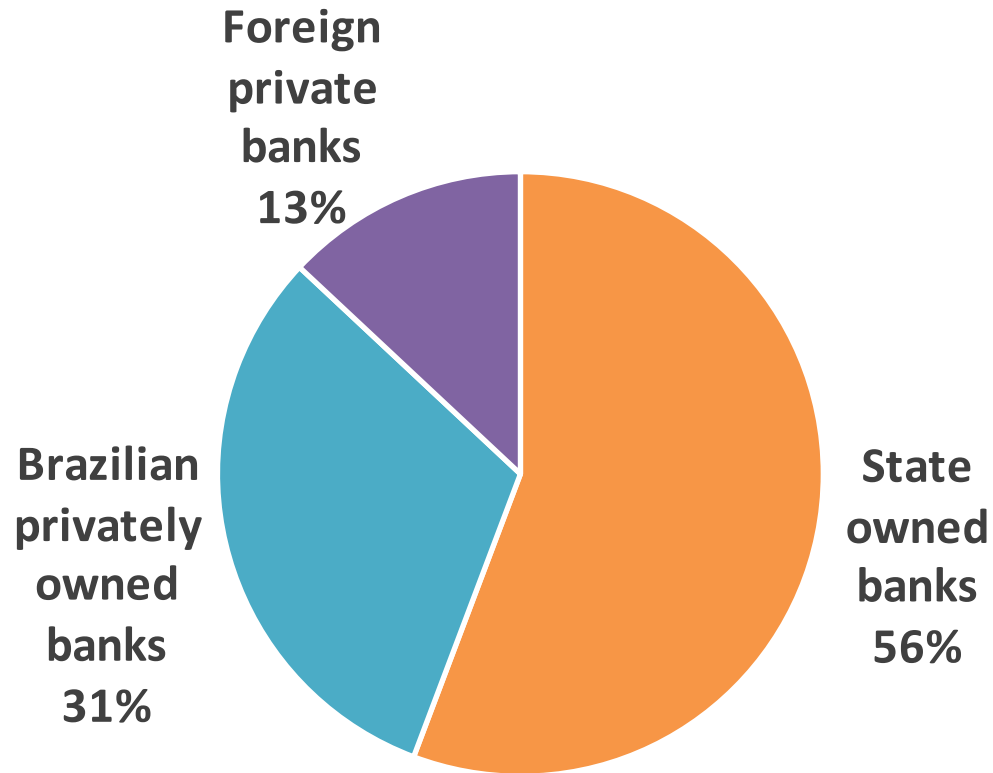


Non-earmarked (RL) x Earmarked (RD) Loans Consumer (PF) x Corporate (PJ) Loans (R\$ Bi)



Credit Market Structure

Share in Total Credit – State owned banks X Brazilian private banks X Foreign private banks in 2016

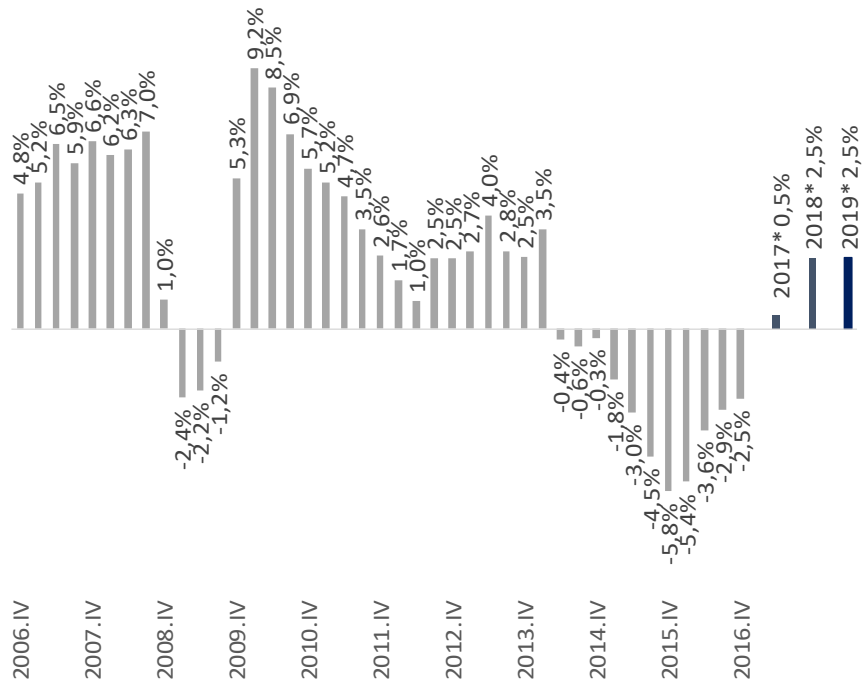


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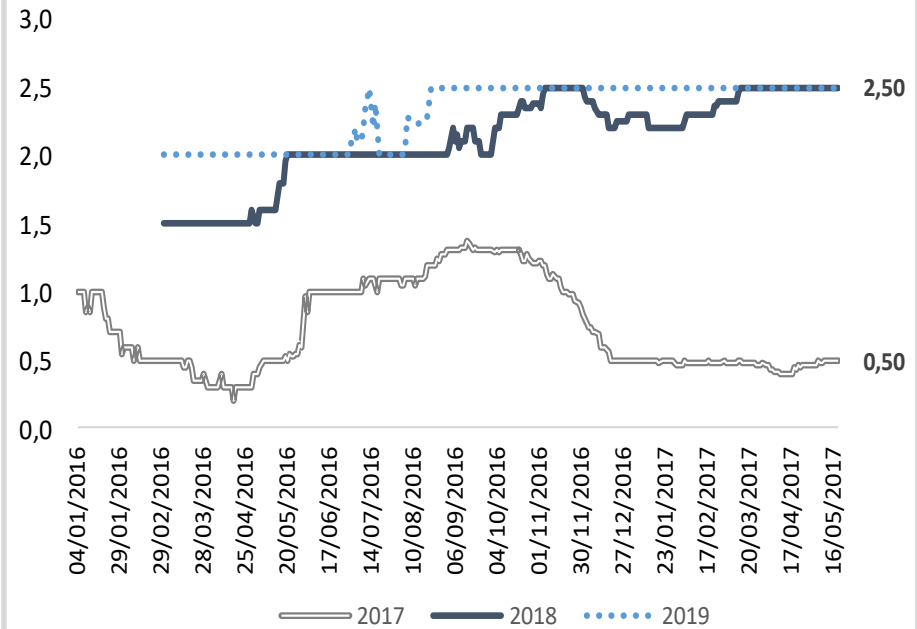
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Economic Activity: end of recession seems near

GDP (% Y/Y)

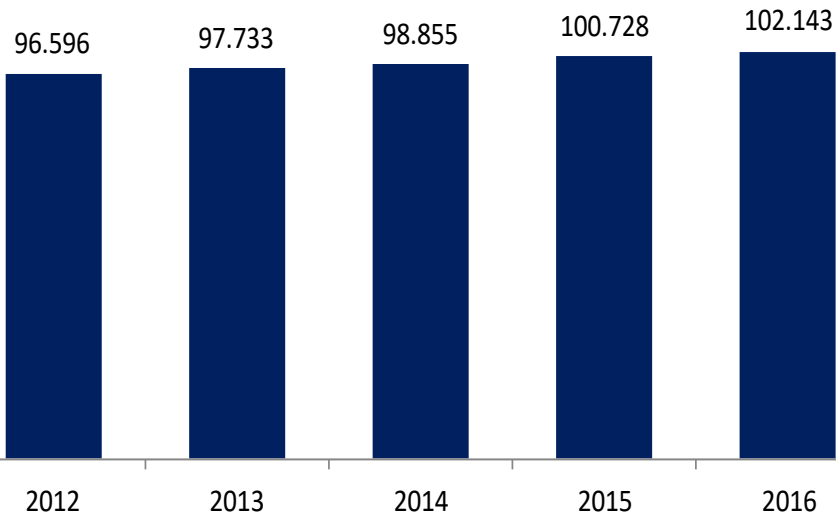


Market Expectation* - GDP (% Y/Y)

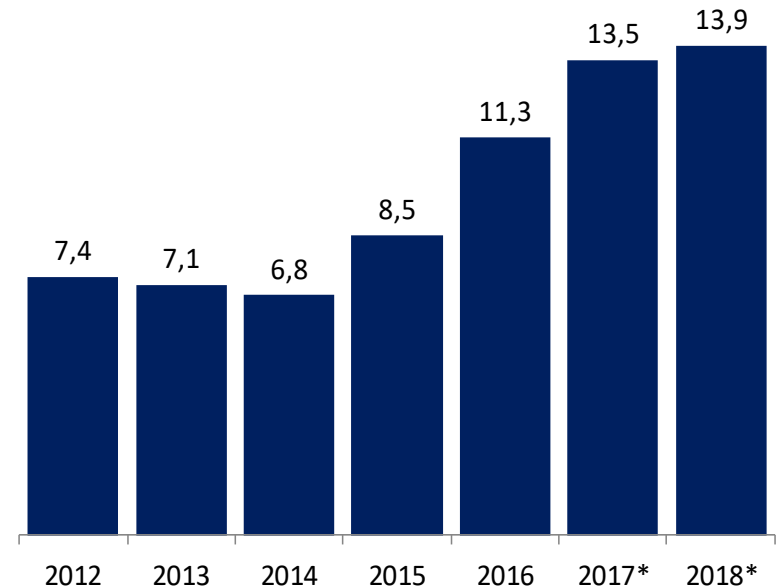


Economically Active Population (EAP) and Unemployment Rate

Economically Active Population (Thousands)

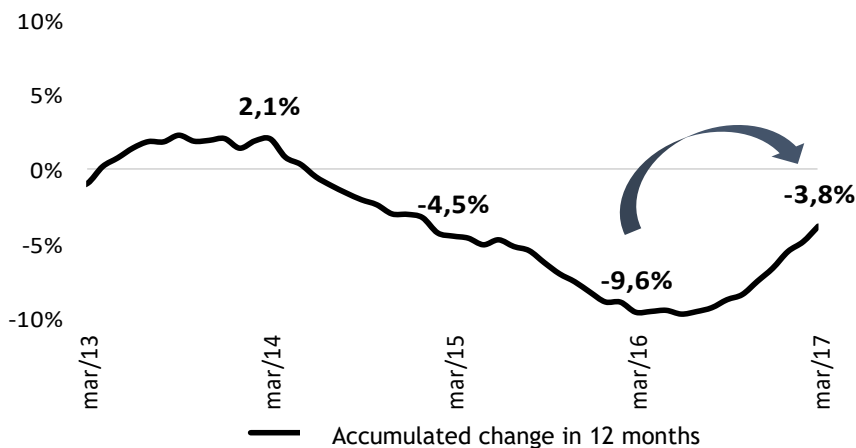


Unemployment* (% EAP)

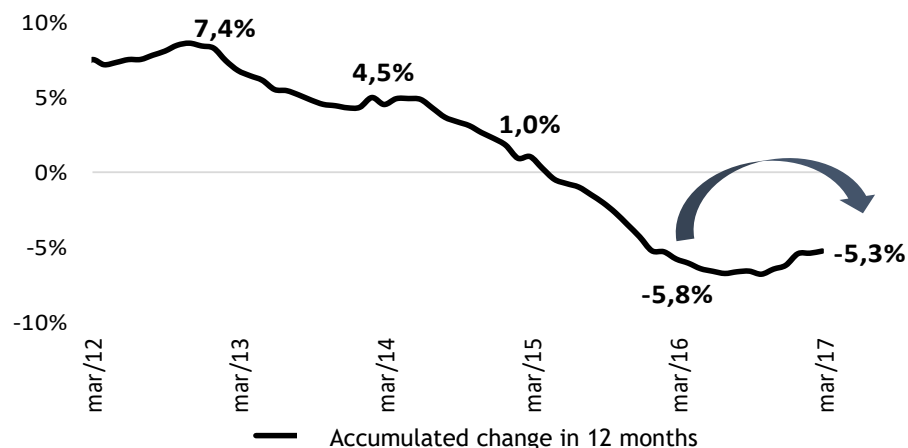


Industry, Retail Sector, Income and Employment

Industrial Production (12m)

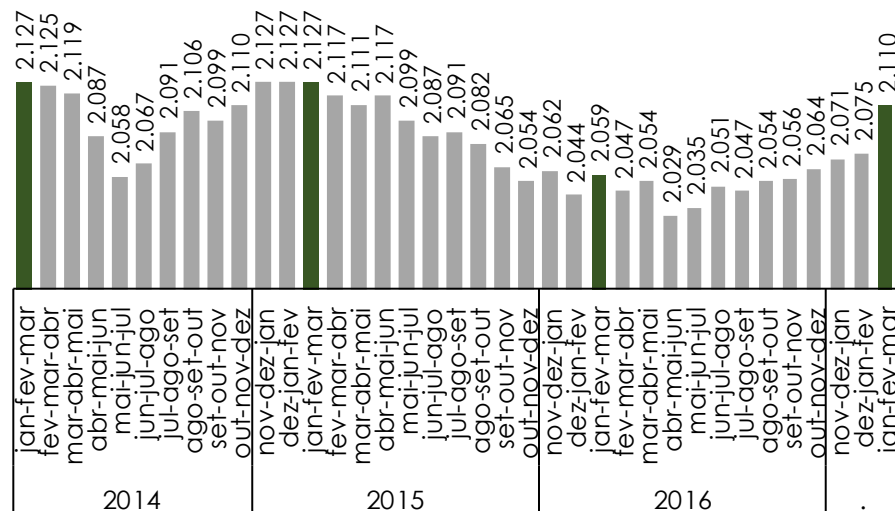


Core Retail Sector Sales (12m)



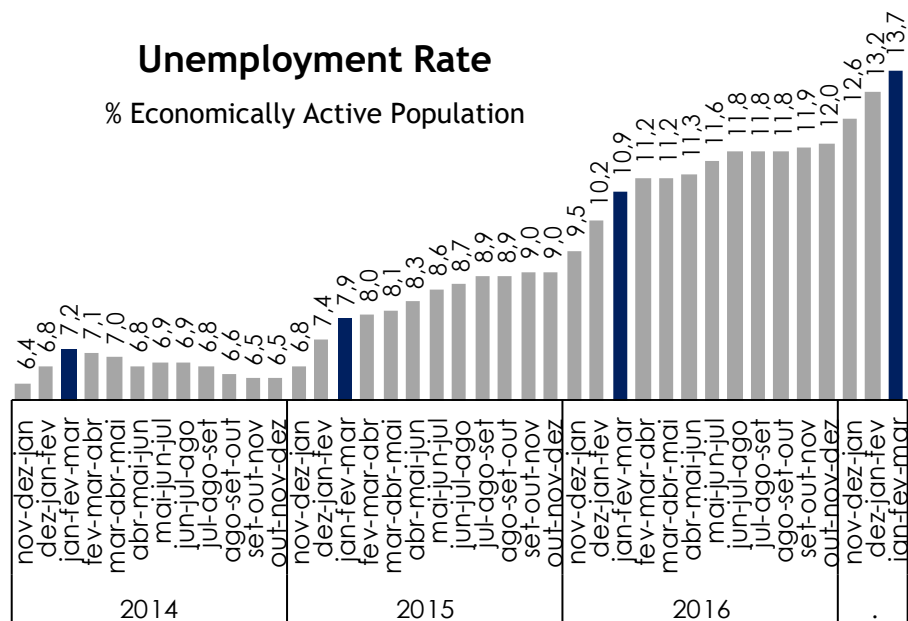
Average wage

Employees aged 14 and over during the reference week
(constant prices at 2017 R\$)



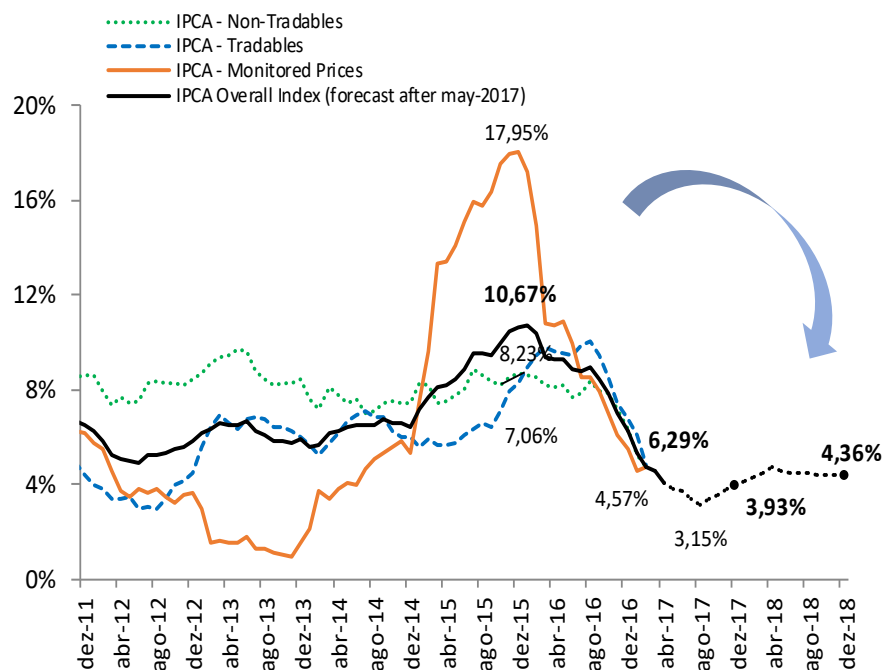
Unemployment Rate

% Economically Active Population

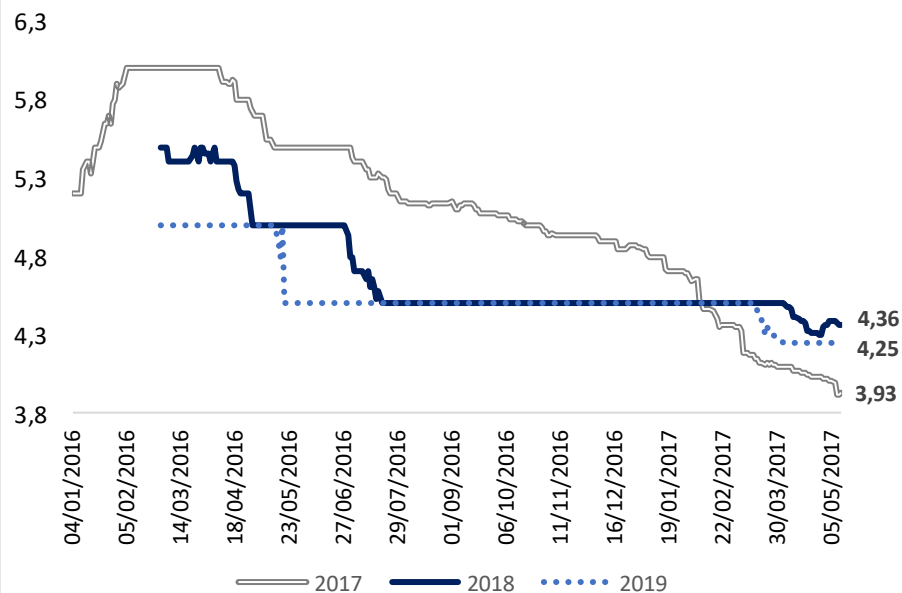


Inflation: sharp fall in inflation and reanchoring of expectations

IPCA - breakdown (% accum. in 12 months)

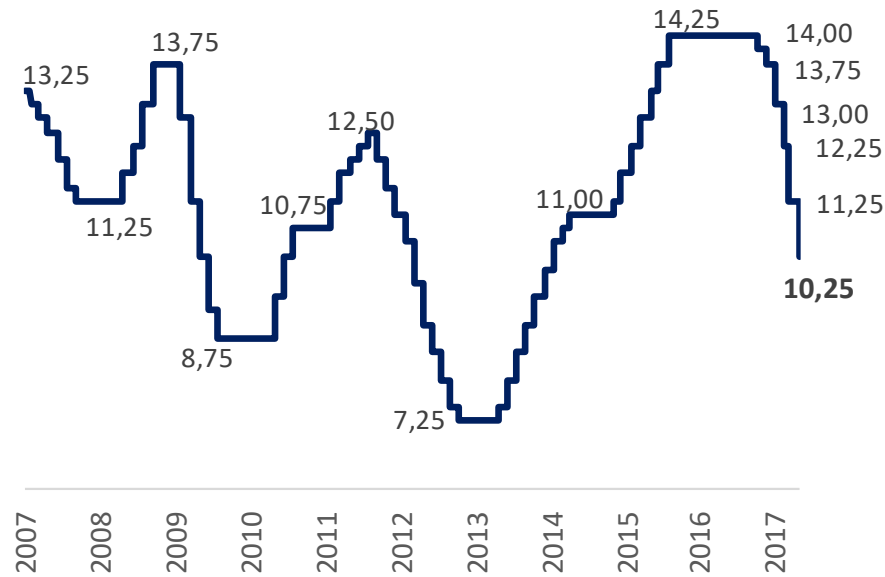


Market Expectation* - IPCA (% Y/Y)

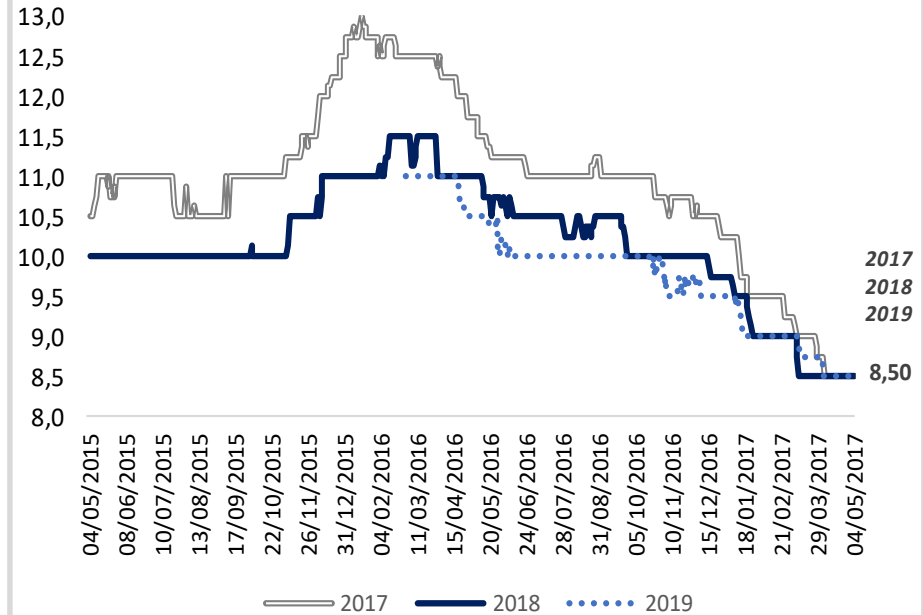


Monetary Policy: fast loosening cycle expected to last

Benchmark interest rate- Selic (P/A %)

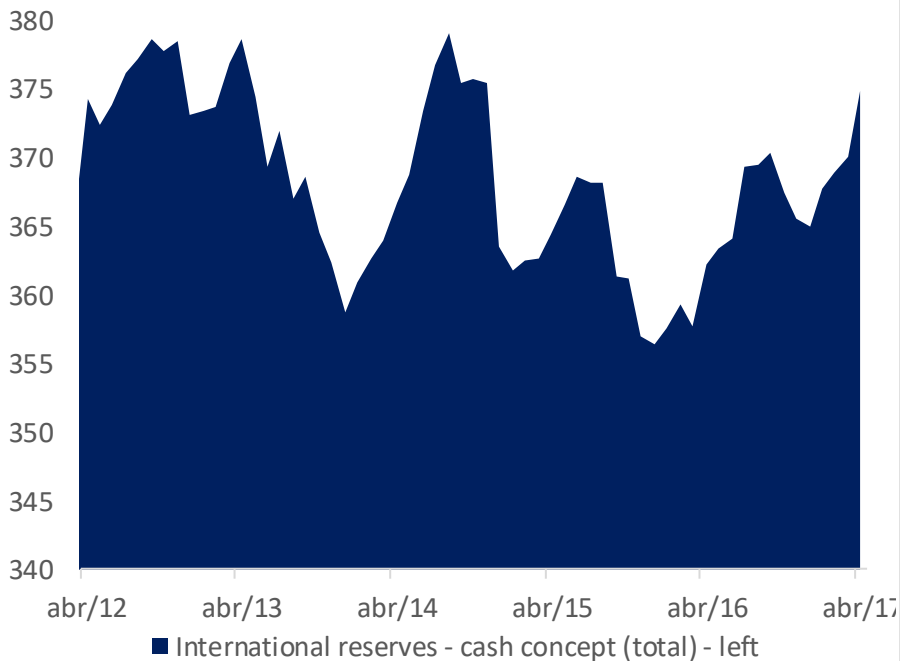


Market Expectation* - Selic (P/A % – end of the period)

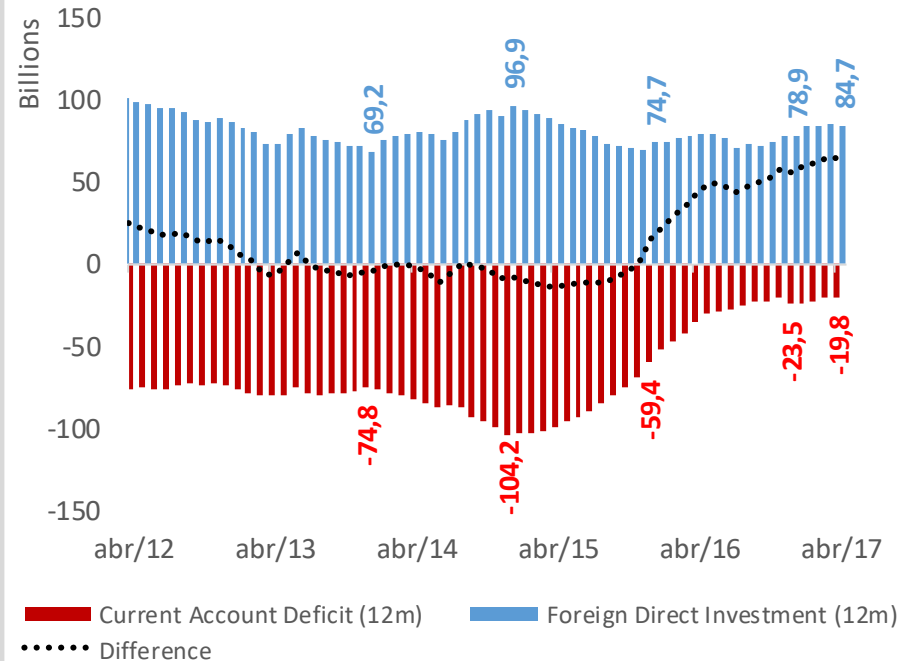


Declining current account deficit fully covered by FDI

International Reserves (US\$ billions)



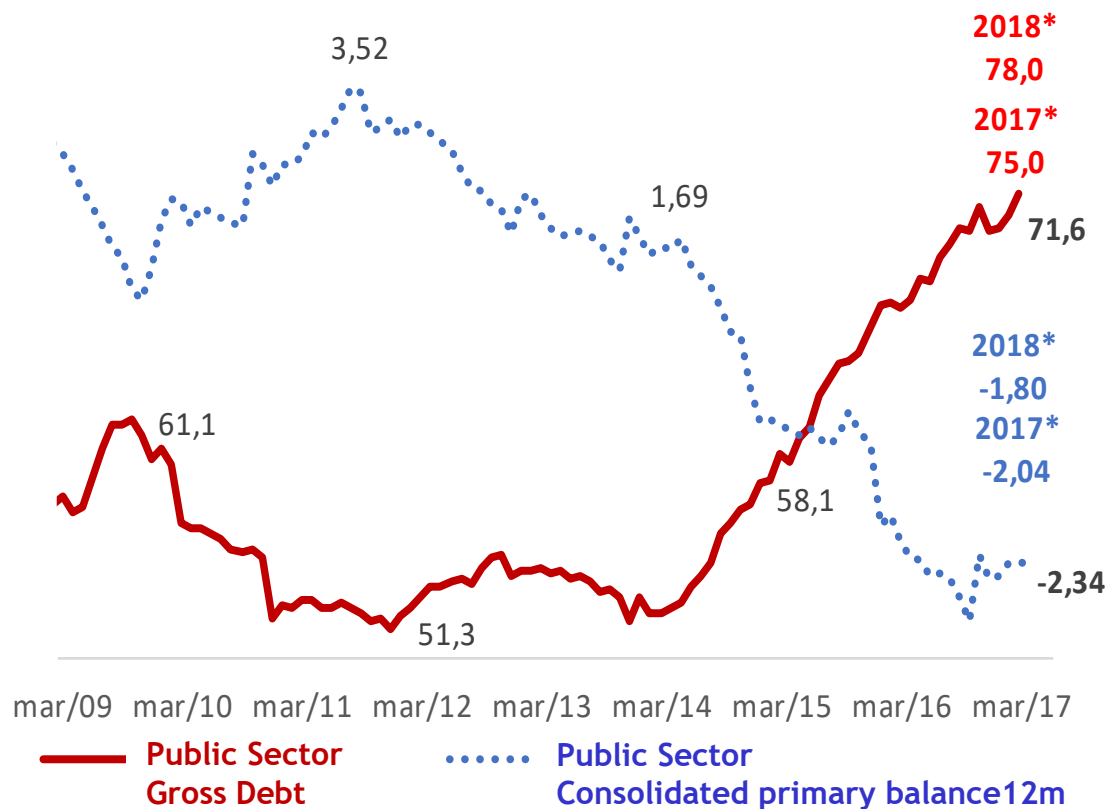
Current Account and FDI (US\$ billions)



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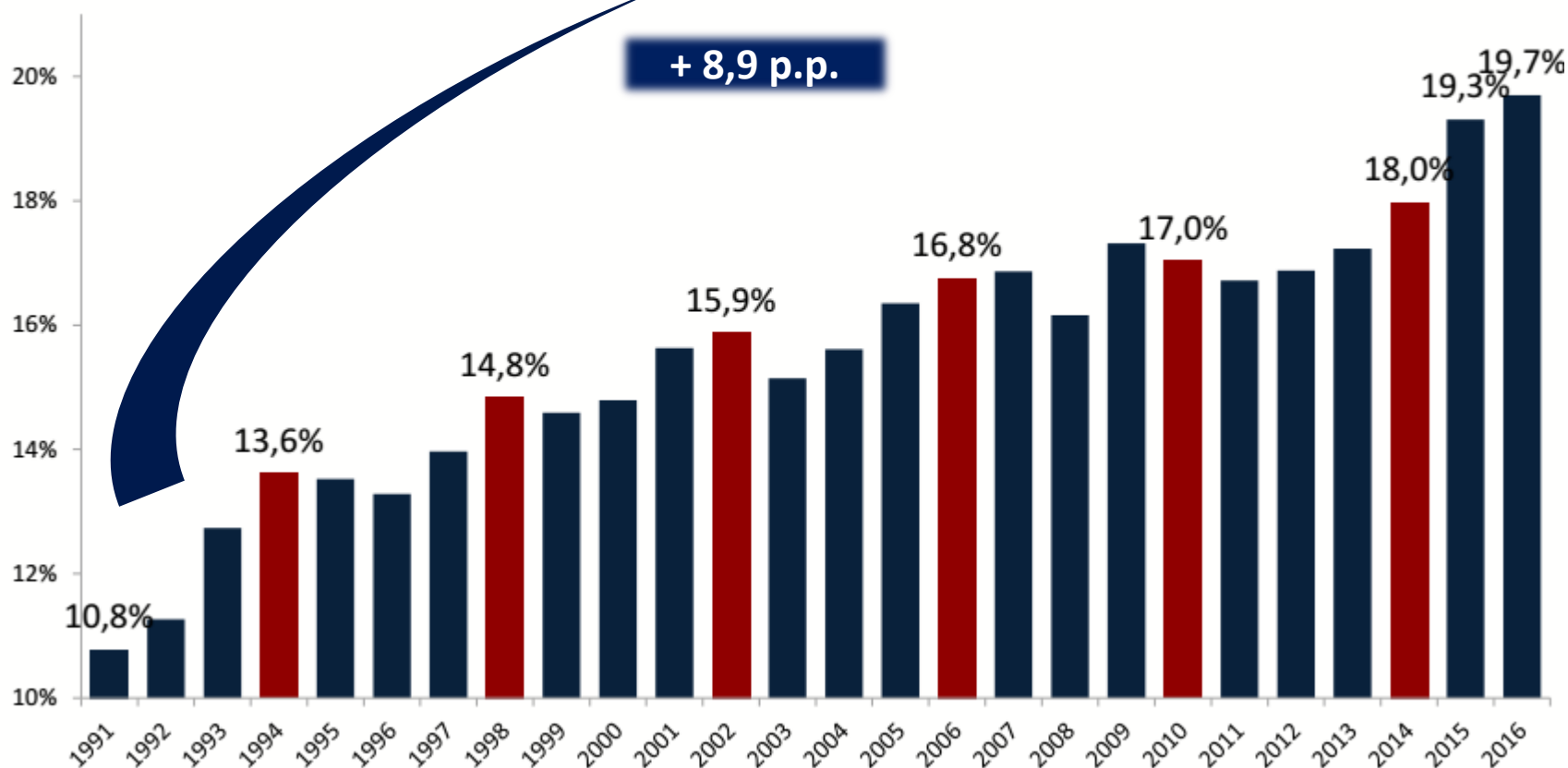
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Gross Debt and Primary Balance (% of GDP)



Evolution of Central Government's Primary Expenditures

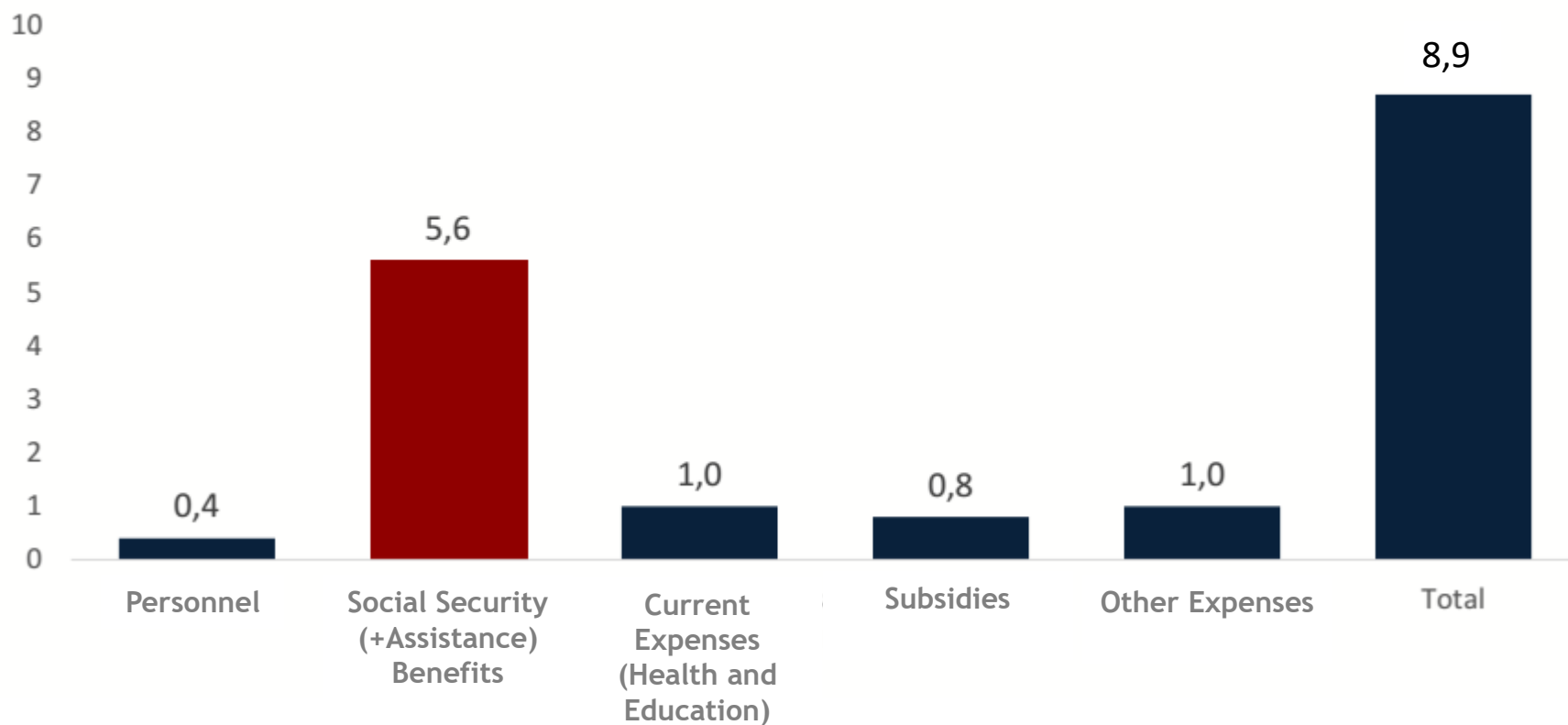
(% GDP)



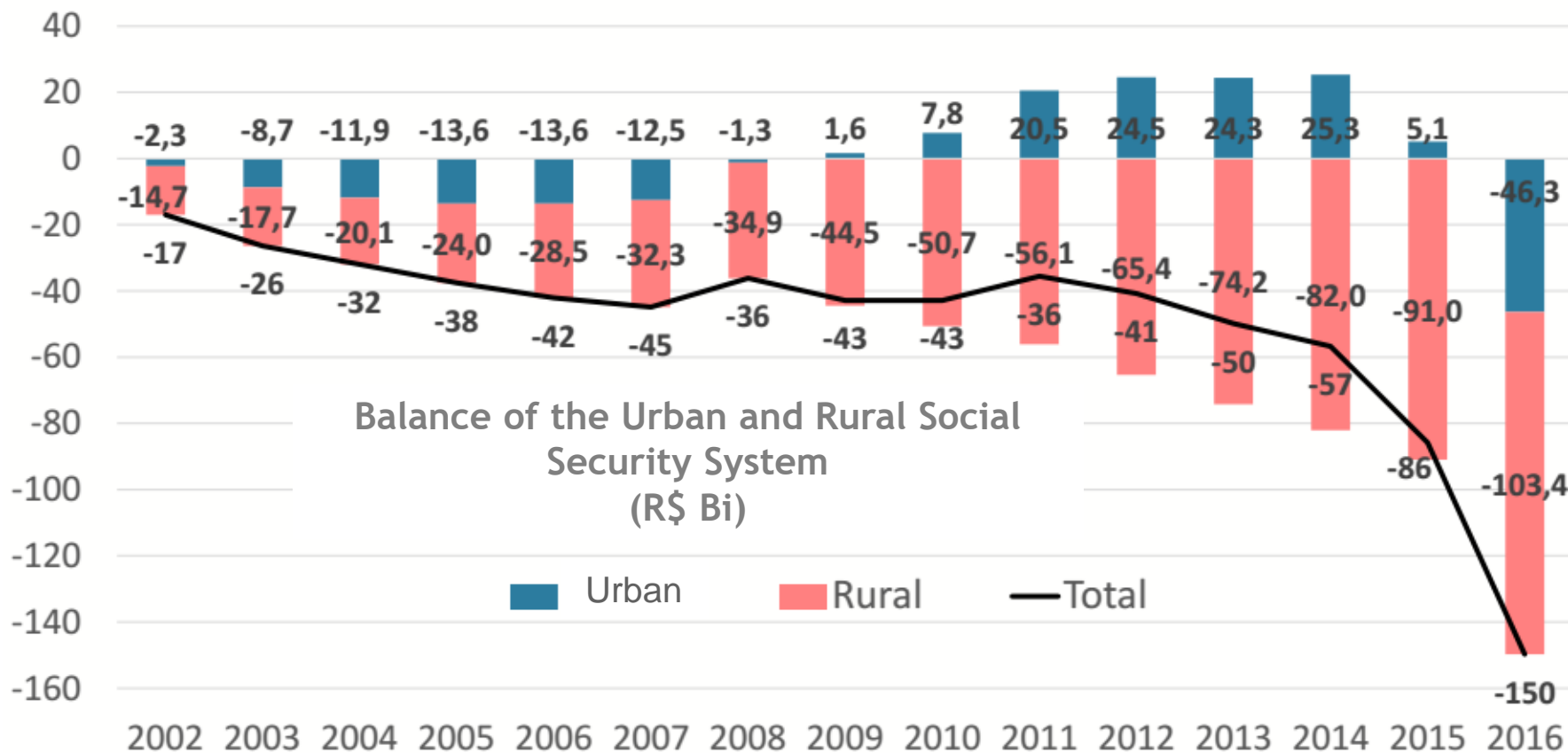
Source: Min. of Finance, SIAFI, IBGE and Mansueto Almeida. *Data from 1991-1996: Giambiagi and Castelar (2012), "Além da Euforia" Translator's Note: Book title freely translated as "Beyond the Euphoria".

Social security is the main reason for higher Primary Expenditures

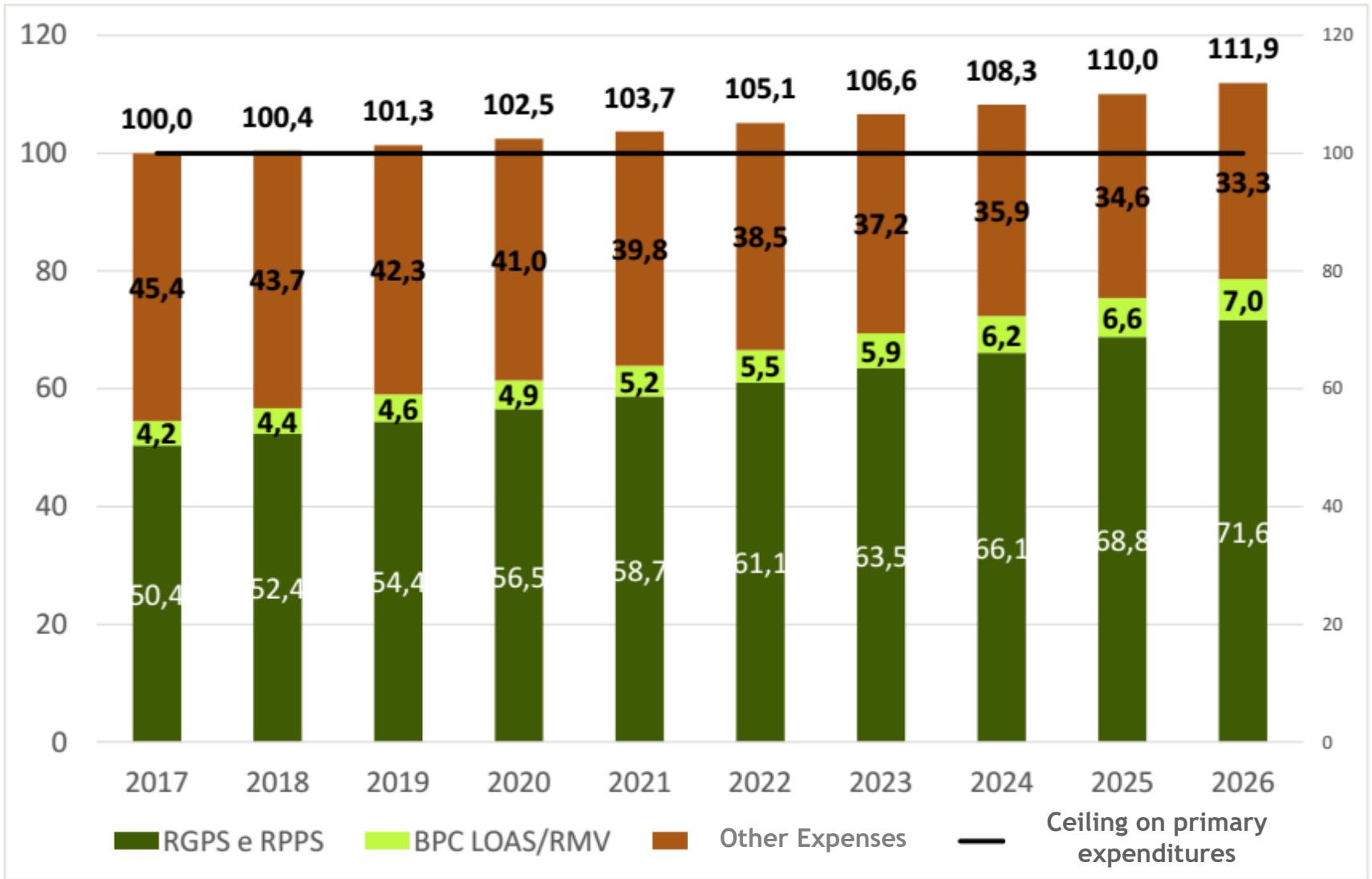
Decomposition of growth in primary expenditure, from 1991 to 2015
(p.p. of GDP)



Social security deficit has been increasing fast



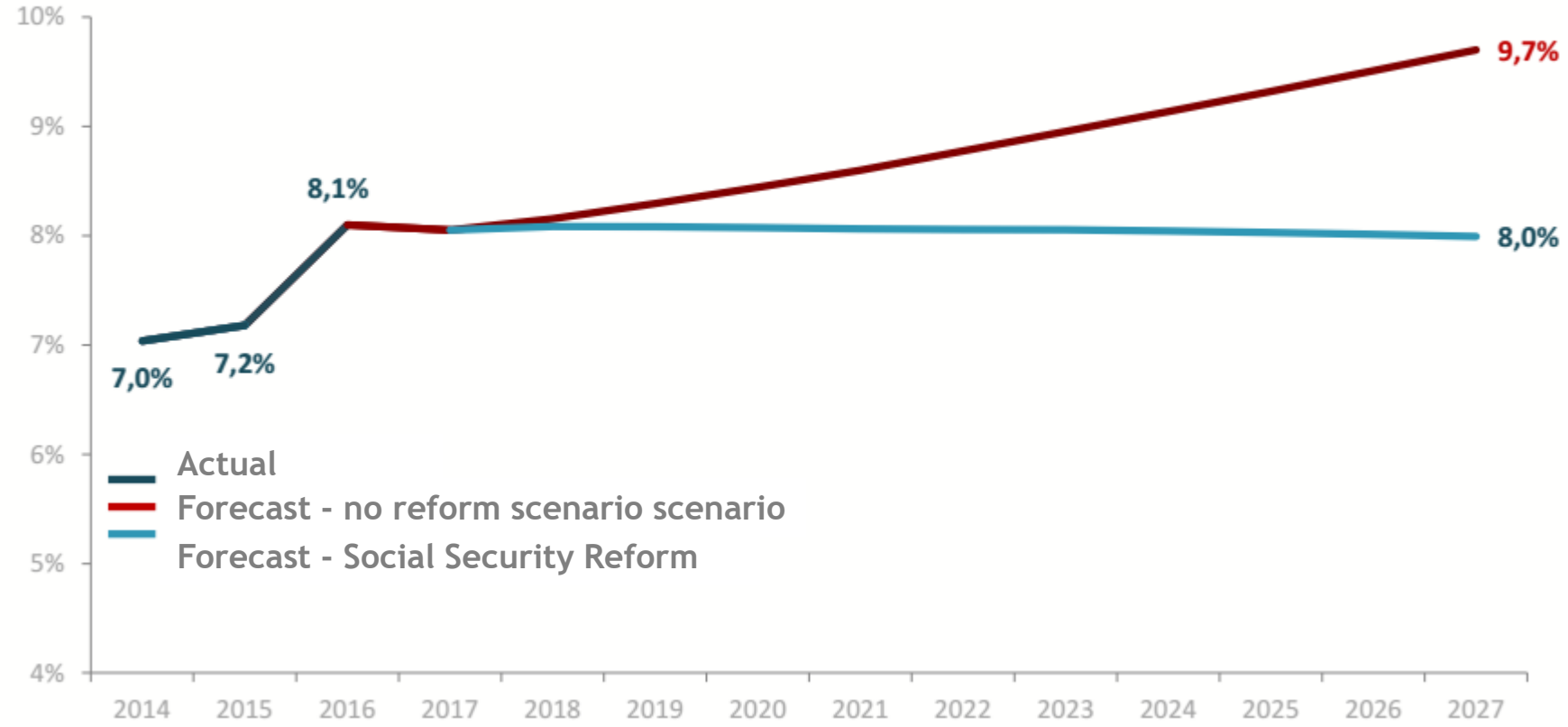
If nothing is done, social security expenditures will squeeze all other expenditures against the Ceiling on expenditure



Source: Min. of Finance, SIAFI, IBGE

Evolution of social security expenditures under reform and no reform scenarios

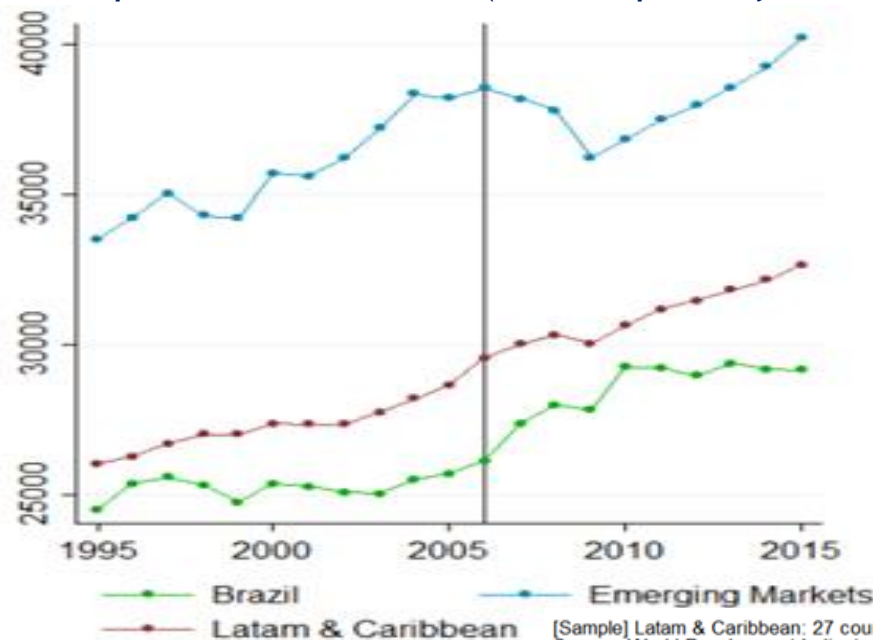
Social Security Benefits (% of GDP)



Business environment and low labor productivity

- Brazil has had historically low labor productivity and slow growth in total factor productivity - TFP
- TFP depends on technological advances, better management, quality of inputs, as well as growth in labor productivity
- Current labor legislation reduces incentives to increase productivity due to legal uncertainty and complexity

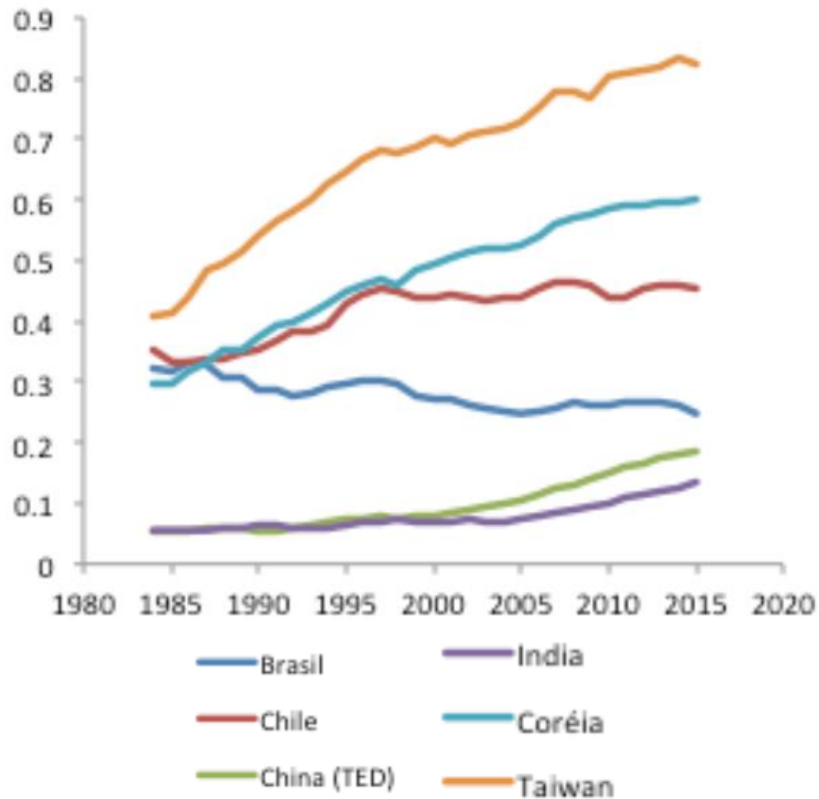
GDP per worker - 1995-2015 (constant prices of 2011 in PPP)



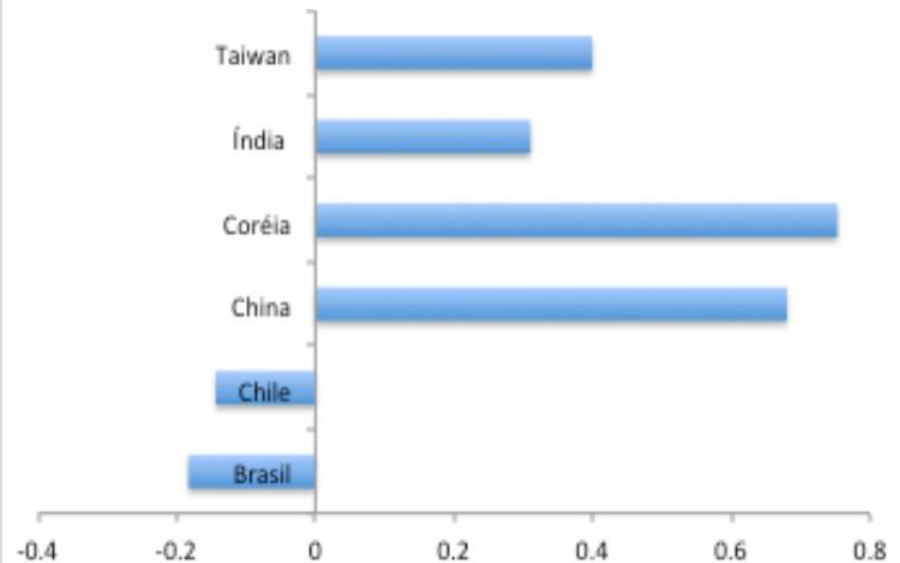
[Sample] Latam & Caribbean: 27 countries. Emerging Markets: 19 countries.
Source: World Development Indicators, World Bank, 2016.

Labor productivity - international comparisons

Product per worker (USA = 1)

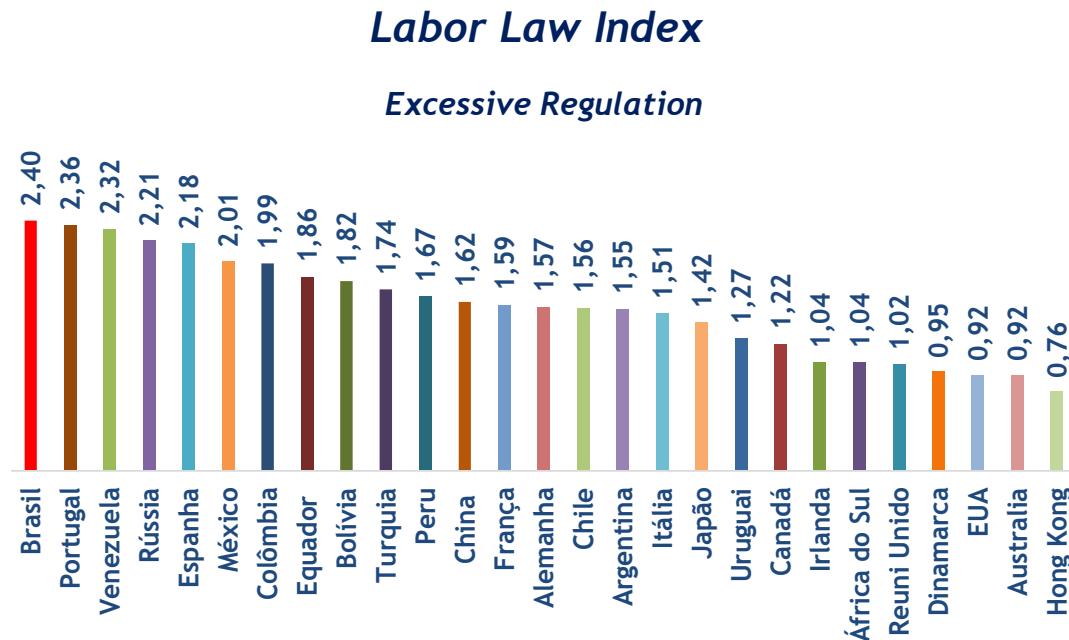


Growth in TFP (in relation to the USA rate since 1980)



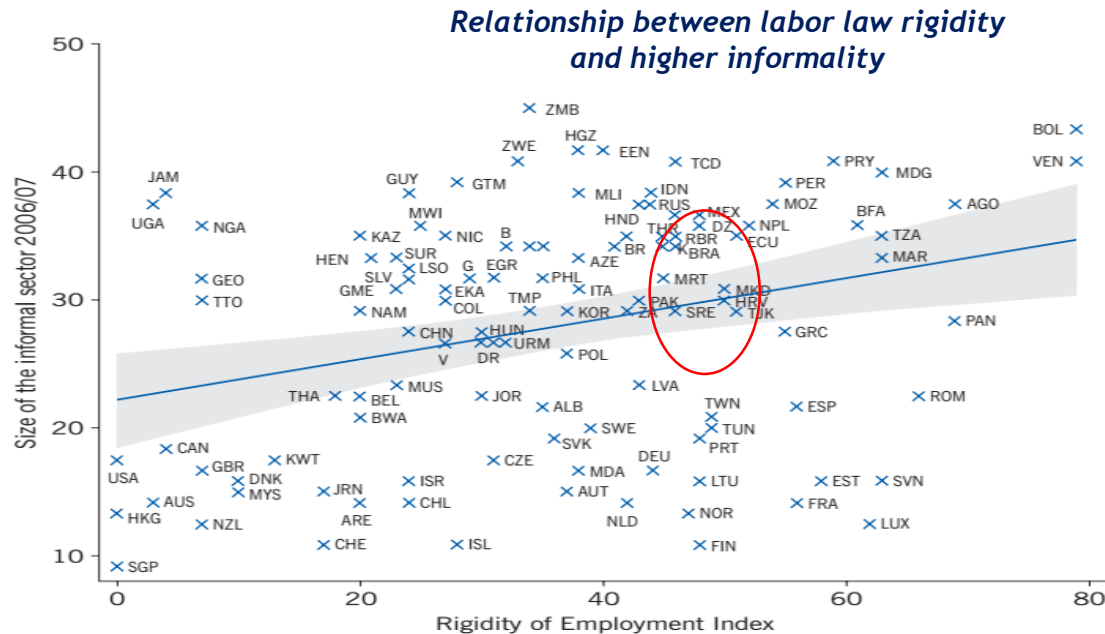
Brazil's labor market is excessively regulated

- In 2003, the National Bureau of Economic Research (NBER) published the labor law rigidity index for 85 countries
 - 1) Rich countries regulate labor less than poor countries
 - 2) Higher regulation levels are associated with informality and high unemployment rates, especially among young people
 - 3) Among the 85 countries analysed, Brazil is the most regulated with negative effects on informality and unemployment



Rigid labor legislation can induce informality

- “In the case of Brazil, the analysis suggests that between 30-40% of the increase in informality can be explained by the increase in labor regulation, including cost of dismissals, through increases in frictional unemployment in the formal sector”
- “In a simulation for the Brazilian case, policies that lowered the cost of formal hiring (reduction in hiring and dismissal costs) not only increased formal employment and reduced informality, but also reduced the aggregate unemployment rate.”



Muravyev, A. *Employment protection legislation in transition and emerging markets*, IZA World of Labor (2014)

Source: Djankov, S., and R. Ramalho. “Employment laws in developing countries.” *Journal of Comparative Economics* 37:1 (2009): 3–13 [2]. Reprinted with permission from the Association for Comparative Economic Studies.

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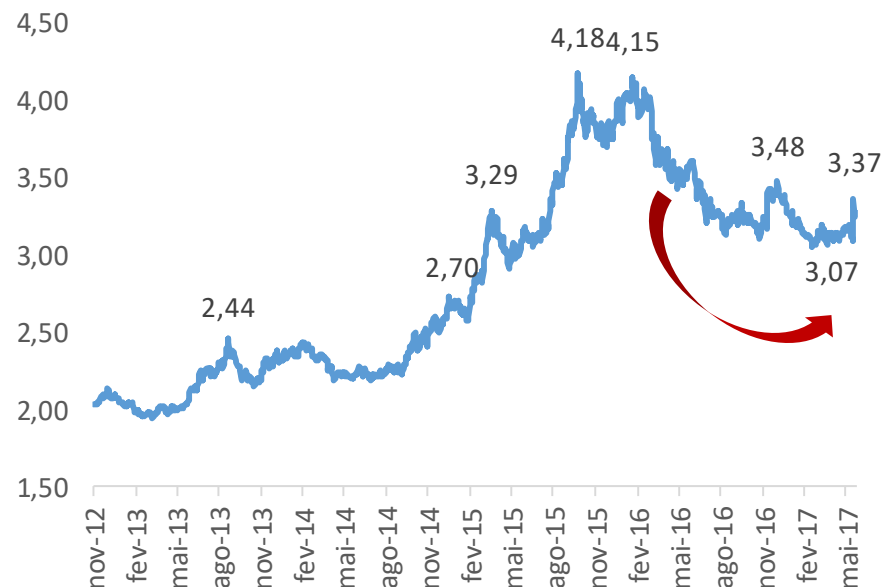
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Country Risk: improved default risk and appreciation of exchange rate

CDS Spread (bps 5Y)



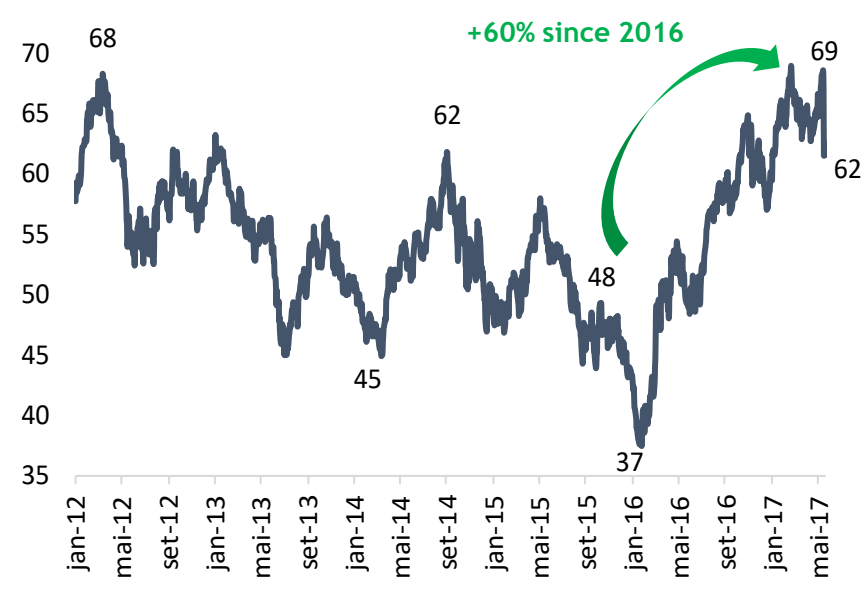
Nominal Exchange Rate (BRL/USD spot rate)



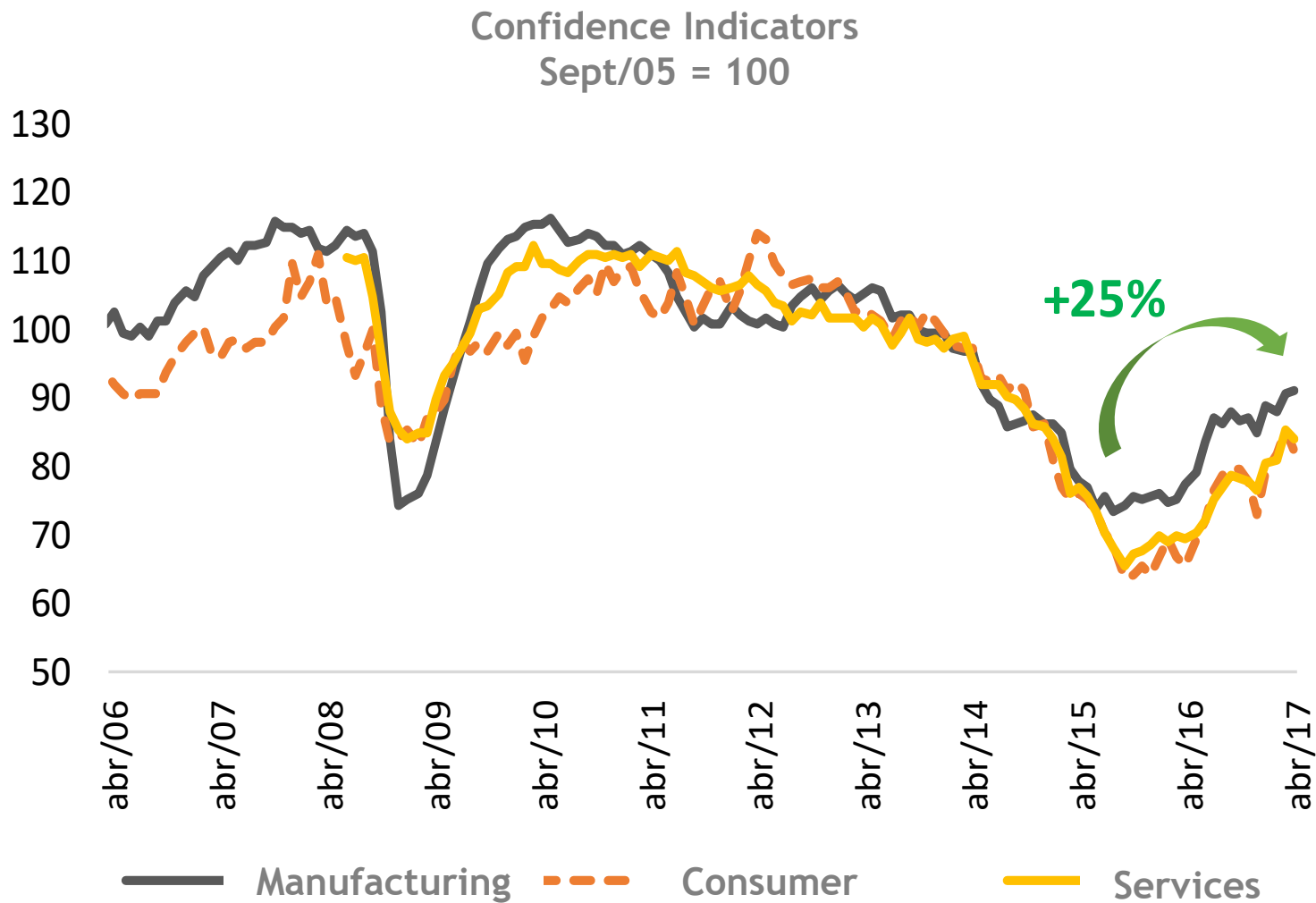
Pre-fixed interest rates (% p.a.)



Ibovespa Index (1000 points)



Confidence indicators show considerable recovery since beginning of Temer government



Baseline Economic Scenario

BCB Focus - Market Readout

	2011	2012	2013	2014	2015	2016	2017	2018
GDP (%)	4,0	1,9	3,0	0,5	-3,8	-3,6	0,5	2,5
Industrial Production (%)	0,4	-2,3	2,1	-3,0	-8,2	-6,6	1,3	2,5
*FEBRABAN Survey - Nominal credit balance - Business Loans (%)	18,9	16,2	13,2	9,5	6,3	-9,5	0,8	6,0
*FEBRABAN Survey - Nominal credit balance - Personal Loans (%)	18,6	16,7	16,0	13,3	7,1	3,2	3,2	6,4
Consumer Price Index - IPCA (%)	6,5	5,8	5,9	6,4	10,7	6,3	4,0	4,4
IGP-M (%)	5,1	7,8	5,5	3,7	10,5	7,2	2,1	4,5
Exchange Rate (R\$/US\$) (end of period)	1,88	2,04	2,34	2,66	3,90	3,26	3,25	3,37
Selic Rate (% p.a.) (end of period)	11,0	7,25	10,00	11,75	14,25	13,75	8,50	8,50
Net Debt of the Public Sector (% GDP)	34,5	32,2	30,5	32,6	35,6	46,2	51,5	55,2
Trade Balance (US\$ billion)	27,6	17,4	0,4	-6,6	17,7	45,0	56,2	43,1
Current Account (US\$ billion)	-77,0	-74,2	-74,8	-104,2	-59,4	-23,5	-23,0	-37,0
Foreign Direct Investment (US\$ billion)	101,2	86,6	69,2	96,9	74,7	78,9	79,0	78,8



BRAZILIAN FEDERATION OF BANKS

Thank you!