Economic Policy and Growth Perspectives

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Finance Minister

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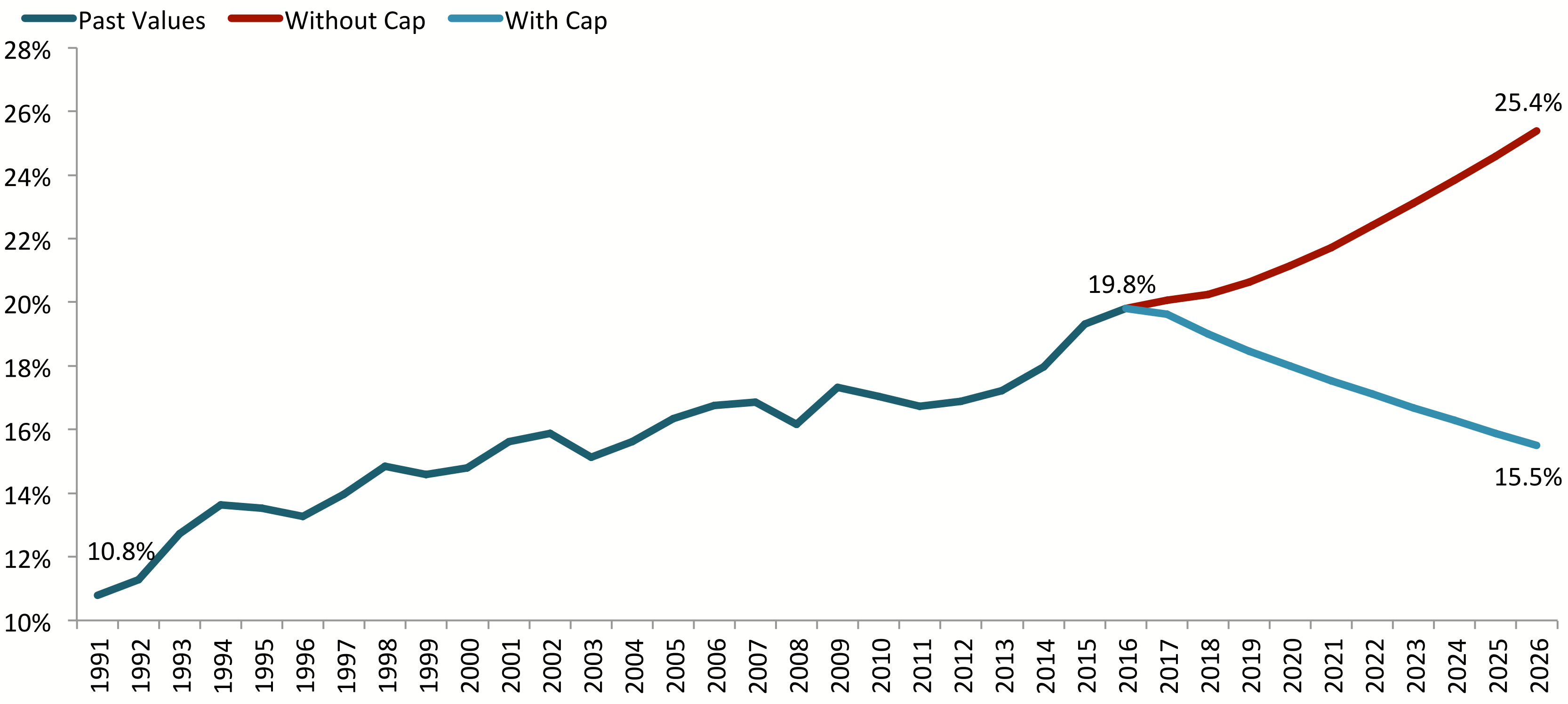
Ministry of
Finance

Fiscal adjustment as necessary condition

Primary Expenditure Trajectory - with and without the Expenditure Cap

Total Primary Expenditure
(% of GDP)



Source: Ministry of Finance, SIAFI, Brazilian Institute of Geography and Statistics (IBGE)

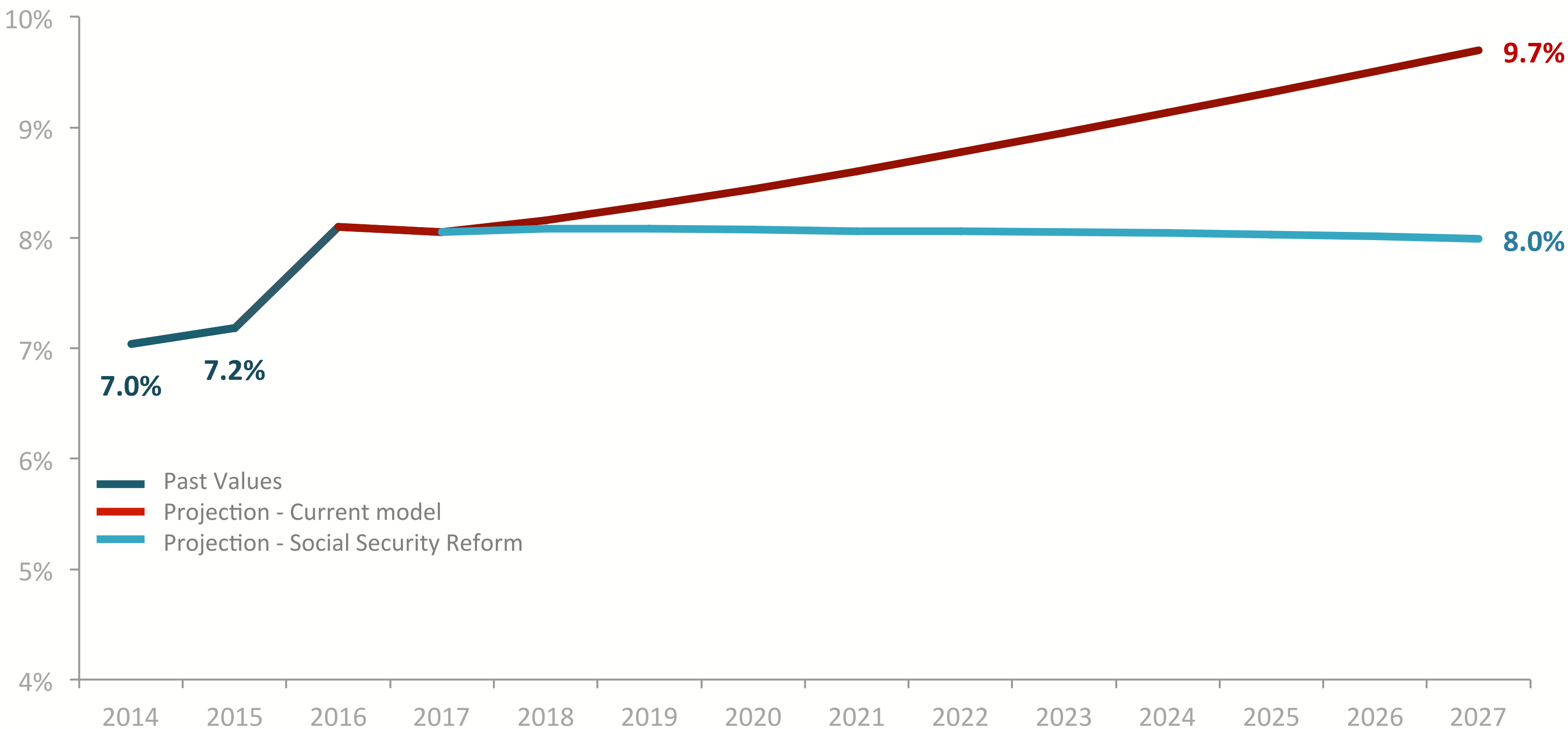
*Data from 1991 to 1996: Gianbiagi e Castelar (2012), "*Além da Euforia*"

** 2010: Does not include Petrobras capitalization

Social Security Reform

A gradual reduction in total expenditure on benefits (% of GDP) will lead to savings of around 1.7 pp of GDP in 2027.

Social Security Benefits
(% of GDP)



Source: Ministry of Finance

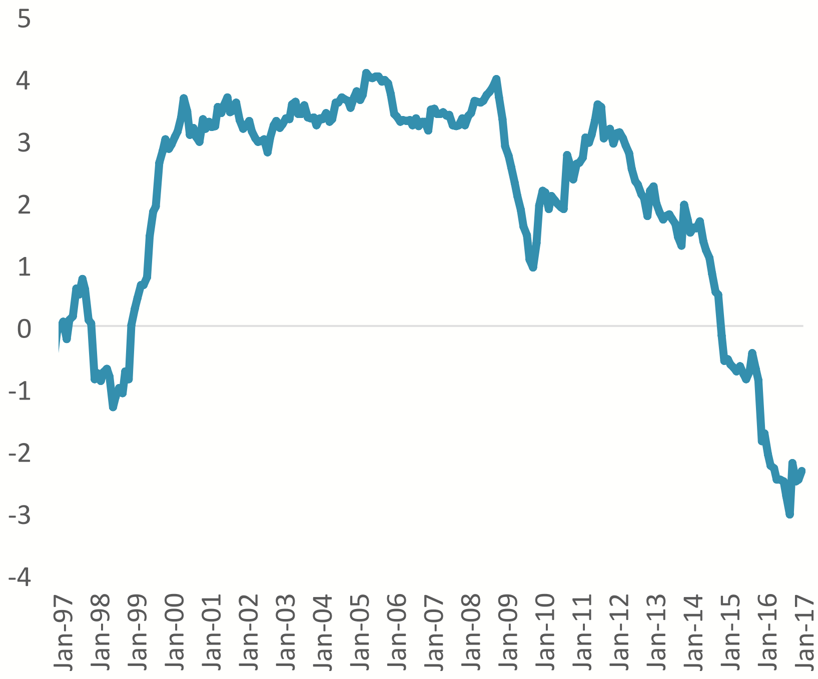
Short Term Growth

Origin of the Crisis

New Economic Matrix and fiscal expansion

Primary balance deficit resulting in debt sustainability problem

Primary Balance
(% of GDP – in 12 months)



Source: Central Bank

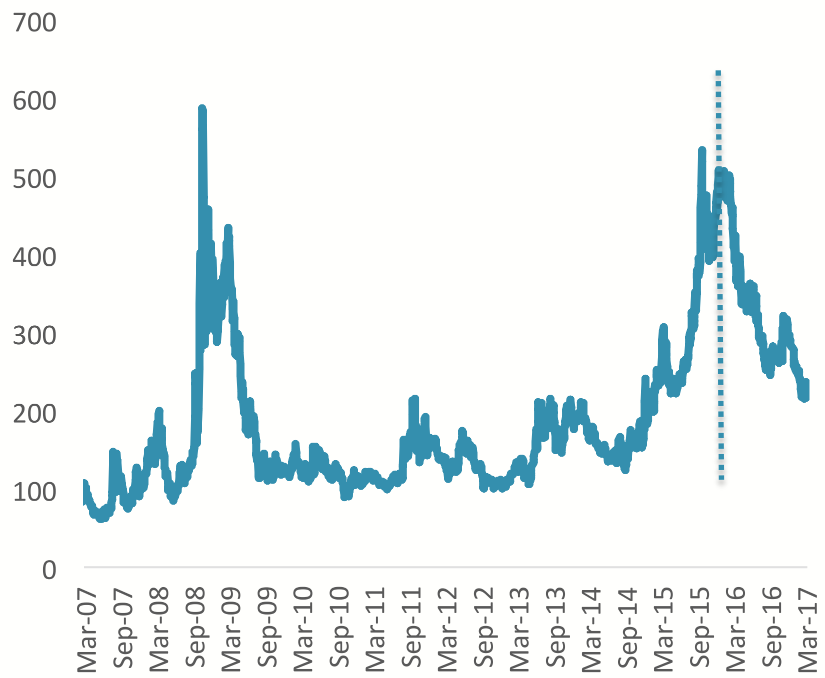
Government Debt
(Gross, % of GDP)

Source: Central Bank

Origin of the Crisis

Sovereign risk soars and Industry confidence collapses
But new Government reverts these trends

CDS – 5 years



Source: Bloomberg

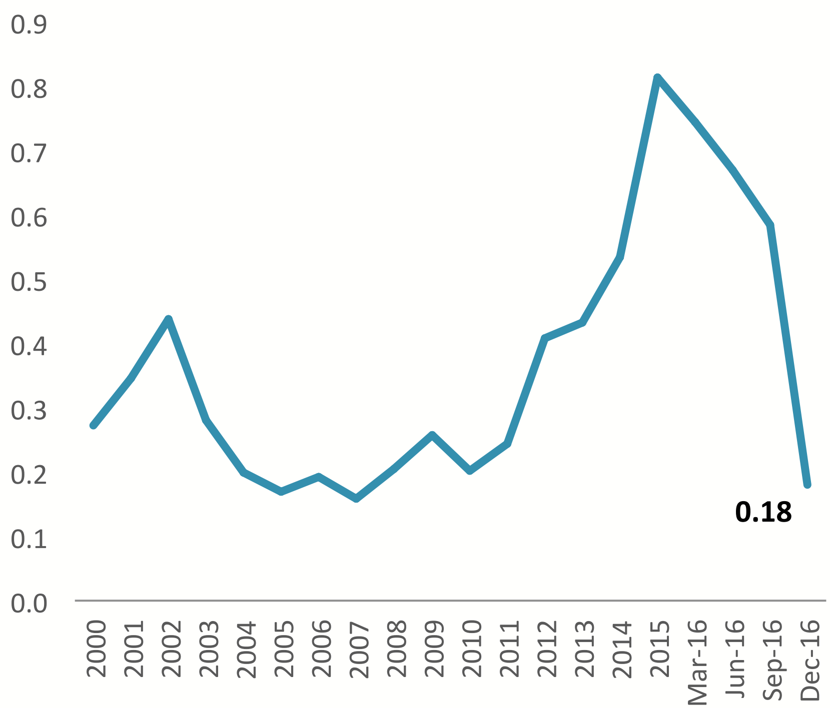
Industry Confidence

Source:FGV

Reasons for Slow Recovery

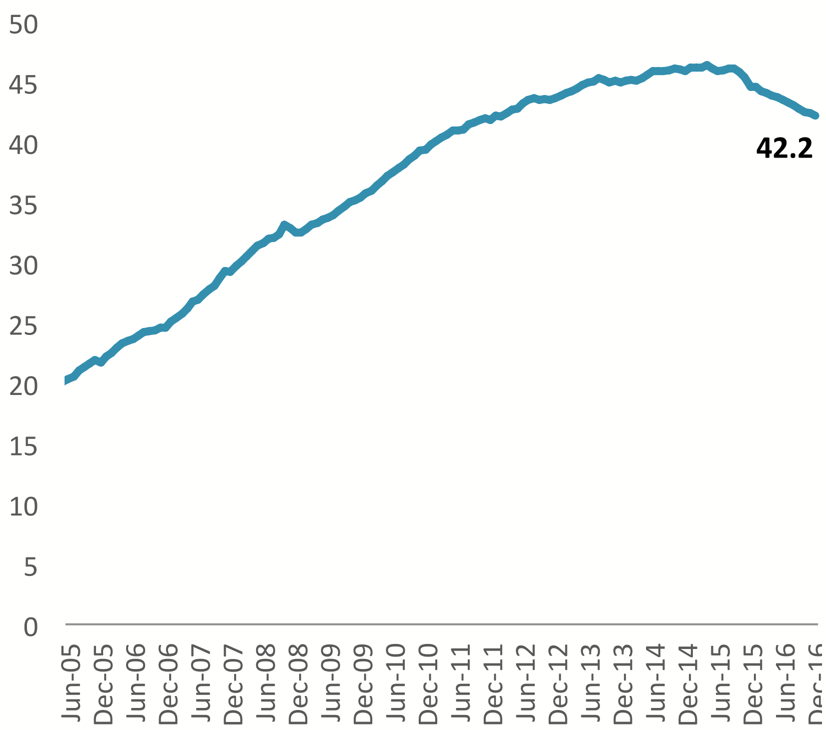
Leverage of firms and families has limited the availability of resources for investment and durable goods consumption. But this is being reversed.

Companies' Indebtedness
(Net debt/ Equity)



Source: Ministry of Finance

Household's Indebtedness
(% of Income)



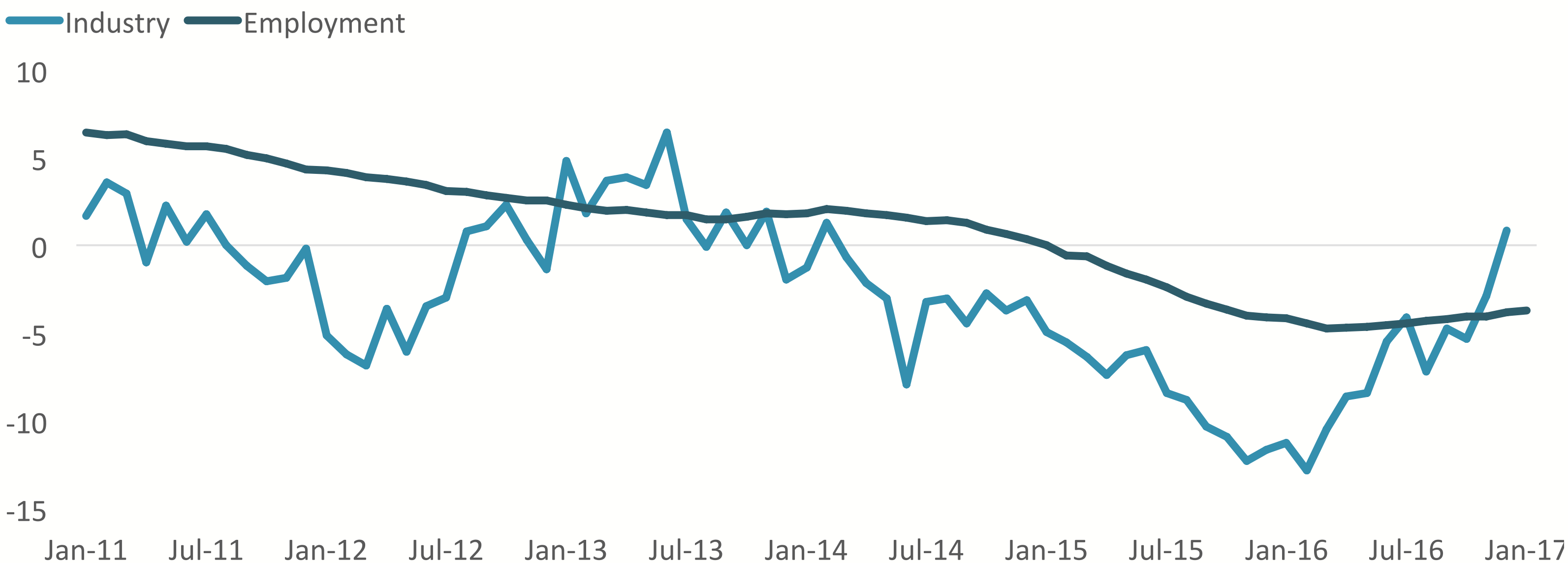
Source: Ministry of Finance

Economic Recovery

With firms and families deleveraging, Expenditure Cap, Social Security Reform and inflation control, the growth is returning.

- **Industry already shows positive yoy growth**
- **Employment, although lagged, has already reversed the trend**

Evolution of Industrial Production and Employment
(Yoy growth - %)



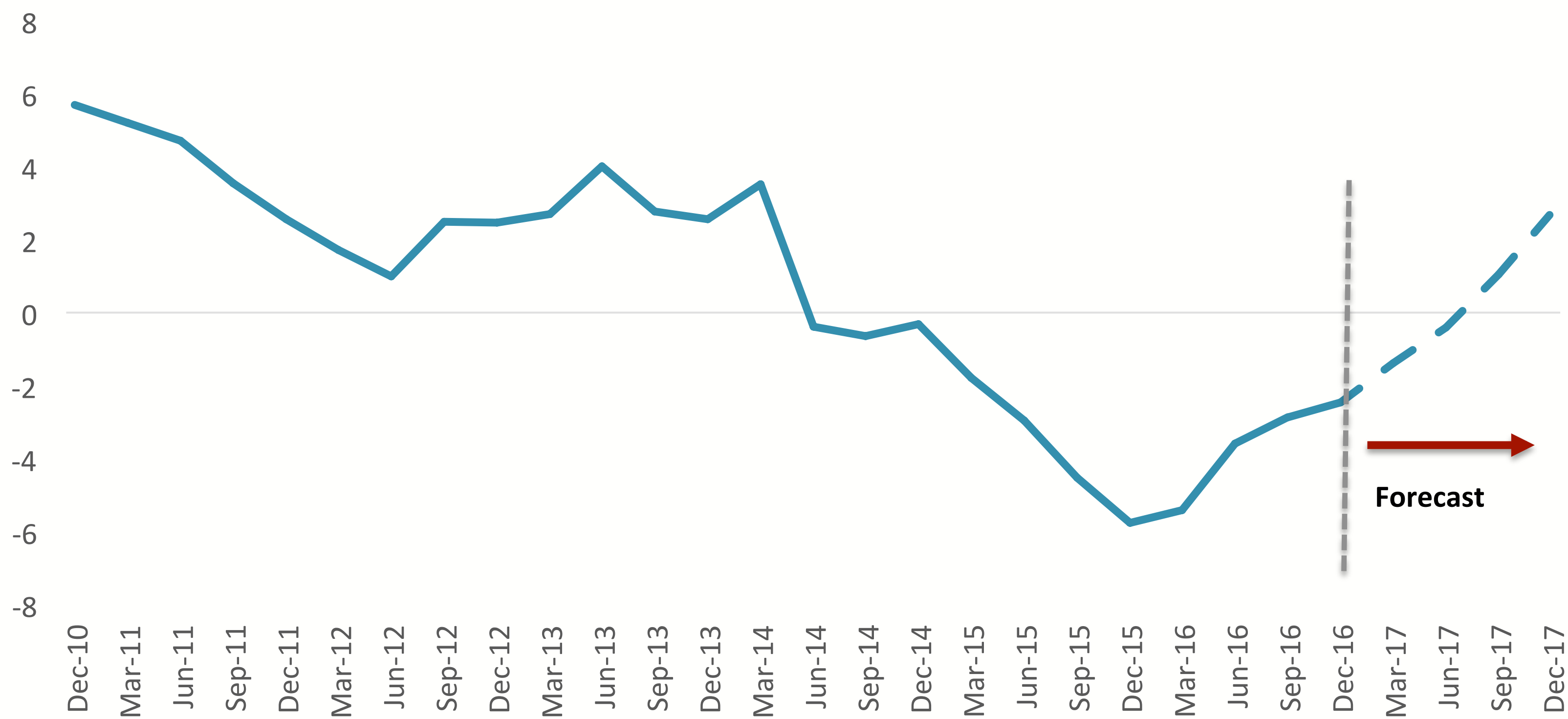
Source: IBGE, RAIS / Elaboration: Ministry of Finance

Economic Recovery

GDP growth in the end of 2017 (4º quarter on 4º quarter of 2016) around 2.7%.

GDP

(Quarter on the same quarter of the previous year - %)



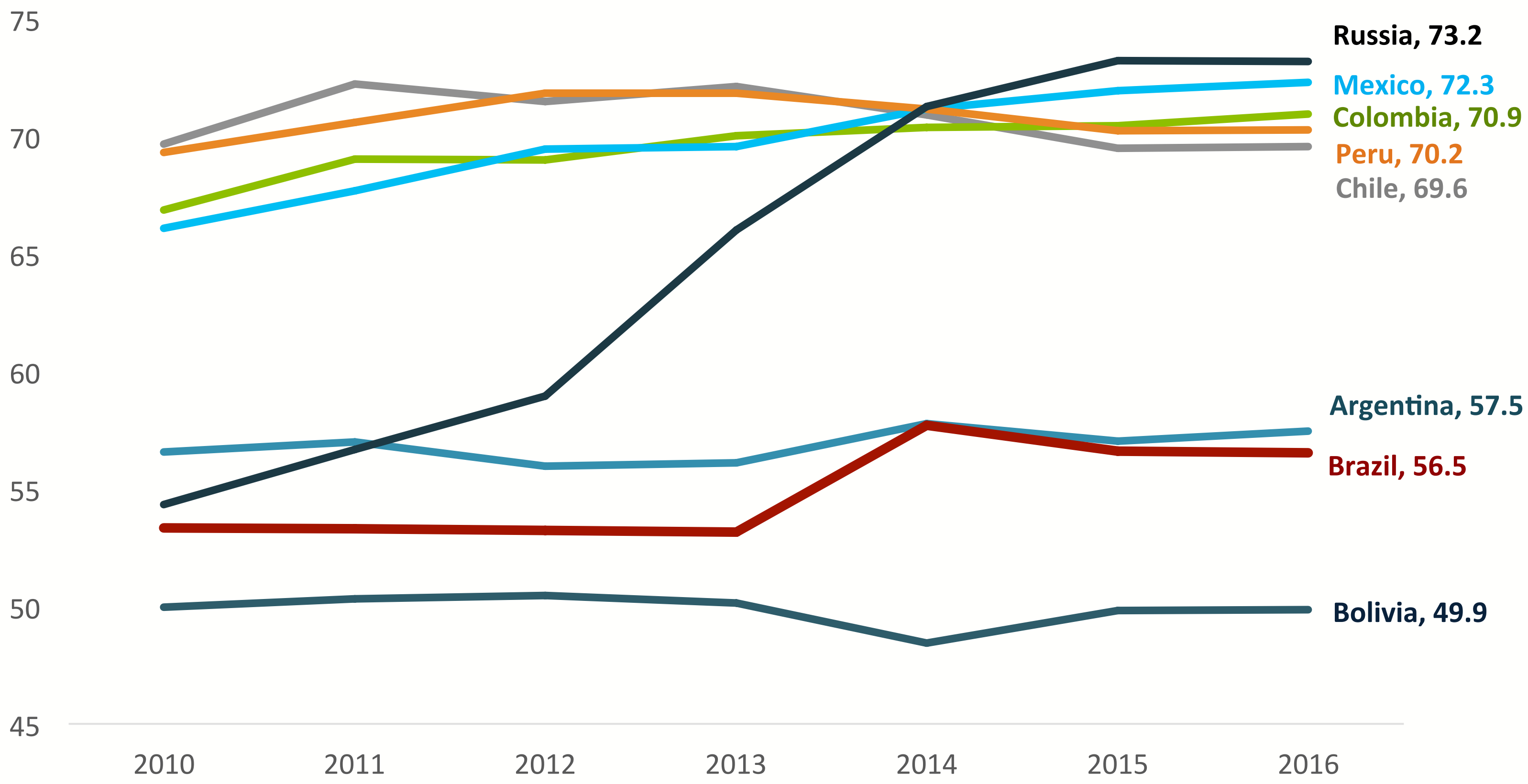
Source: IBGE / Forecast: Ministry of Finance

Productivity Agenda and Long Term Growth

Evolution of the Business Environment in Emerging Economies

Distance from the Border - Business Environment

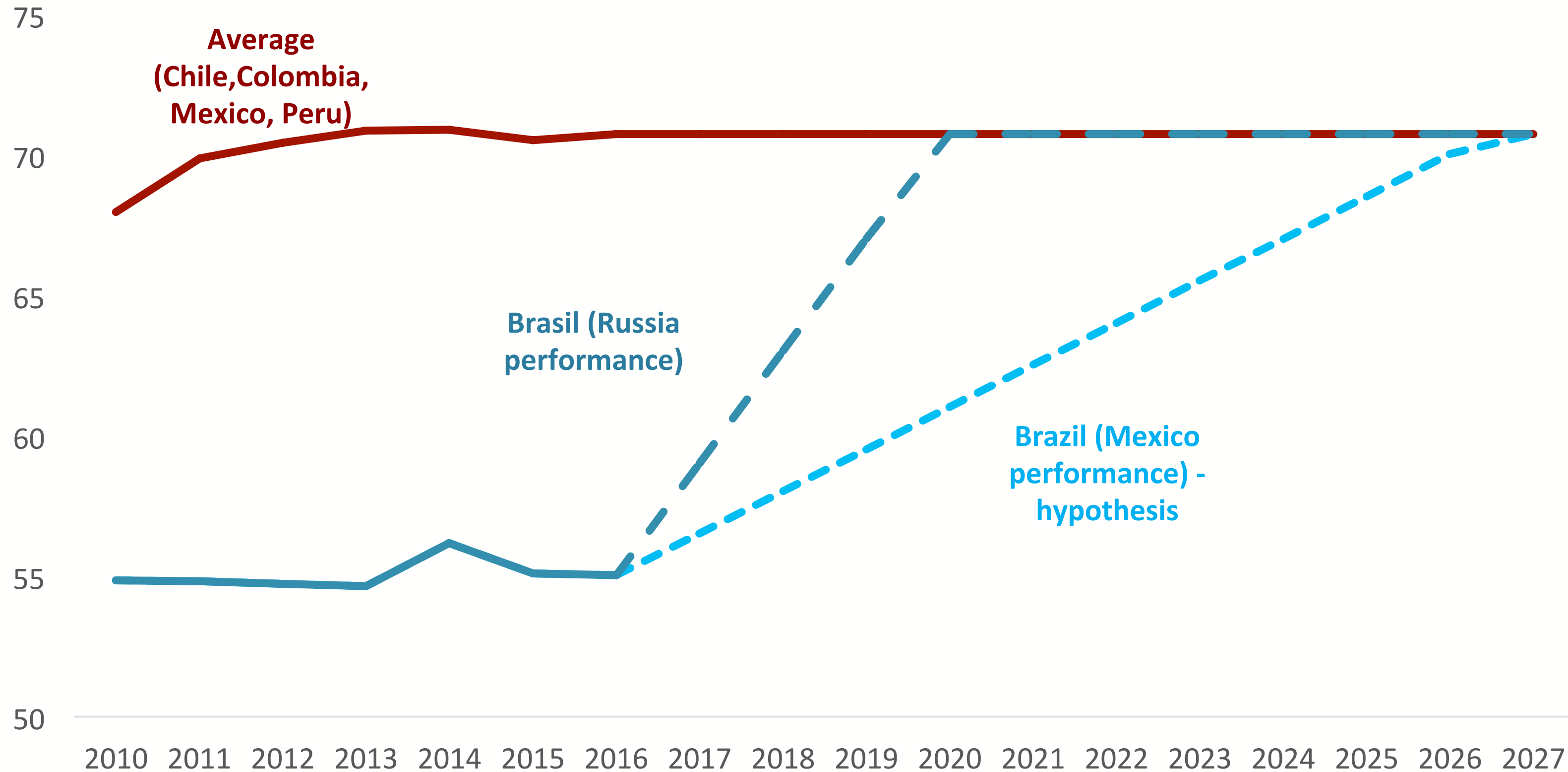
(100 indicates country with the best performance)



Source: World Bank "Doing Business", global indicator

Scenario for Brazil

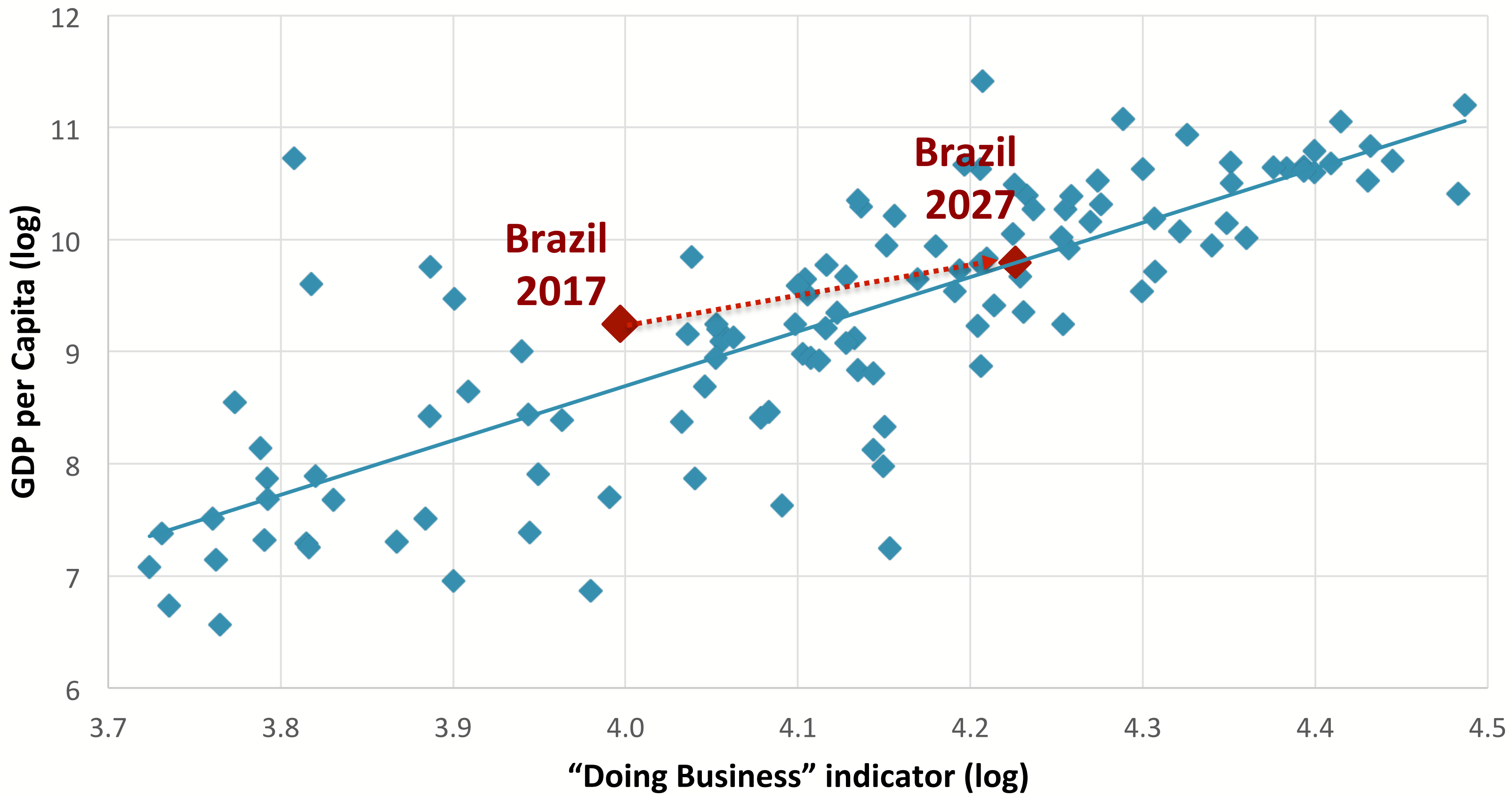
Distance from the Border - Business Environment
(100 indicates country with the best performance)



Source: World Bank "Doing Business", global indicator / Elaboration: Ministry of Finance

Scenario for Brazil

GDP per Capita x Business Environment



Source: World Bank "Doing Business", global indicator / Elaboration: Ministry of Finance

Productivity Agenda

CREDIT RELATED REFORMS

- Creation of consumer's positive credit history (compilation of the available data before authorization)
- Legal certainty to the establishment of a centralized market for receivables (currently decentralized in notaries), to facilitate securitization and to increase competition.
- Improvement in the Bankruptcy Law (empowering creditors, incentivizing extrajudicial recovery, speeding up process)
- "Letra Imobiliária Garantida" (covered bond) - immovable properties instrument which segregates bank risk

→ SPREAD REDUCTION

Productivity Agenda

DOING BUSINESS REFORMS

- Labor Legislation (outsourcing, negotiated vs. legislated, working hours)
- Tax and Registry Automatization and Bureaucracy Reduction
  - e-Social (system for labor related payments)
  - SPED (system for tax registration)
  - Municipalities' electronic fiscal receipts standardization
  - Redesim (program to speed up process of starting a business)

→time spent in tax payments from 2,600 hours/year to less than 600

→time for opening/closing a firm from 101 days to 3 days (in SP)

Productivity Agenda

INTERNATIONAL TRADE AND OPENNESS REFORMS

- **Exports (and Imports) Unified Portal**
- **Electronic Certificate for Economic Operator**

  → reduction of time for documentary compliance in 40%

  (now it costs 4-5 days)

- **Foreign ownership of land**

Productivity Agenda

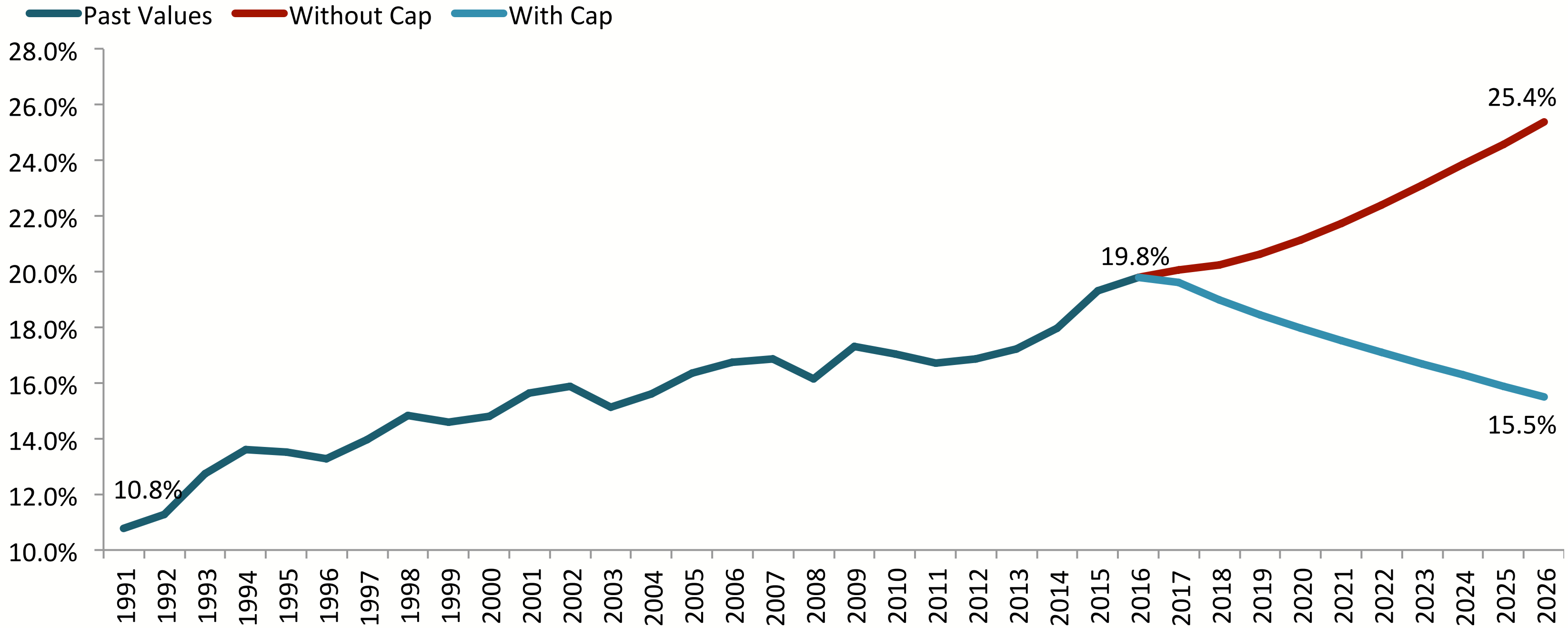
VARIOUS LIBERALIZATION REFORMS

- Realistic concession model, with legal stability and low cost to the Treasury (the transmission line auction as of November 2016 was performed without subsidies).
- Margin of preference in government purchases.
- Oil and Gas Sector reform (horizontalization of national content requirements, allowing reallocation between exploration and distribution sectors)
- State-Owned Companies and Pension Funds Governance
- Recovery of Regulatory Agencies autonomy: agencies will become administrative units with financial independence; directors will need experience and fulfill alternate mandates. The role of a deputy director will be created to avoid vacancy problems.

Remember also the Crowding-In vs. Crowding-Out effect

After almost 30 years of crowding-out (Government pushing private sector out of GDP), there will be crowding-in.

Total Primary Expenditure
(% of GDP)



Source: Ministry of Finance, SIAFI, Brazilian Institute of Geography and Statistics (IBGE)
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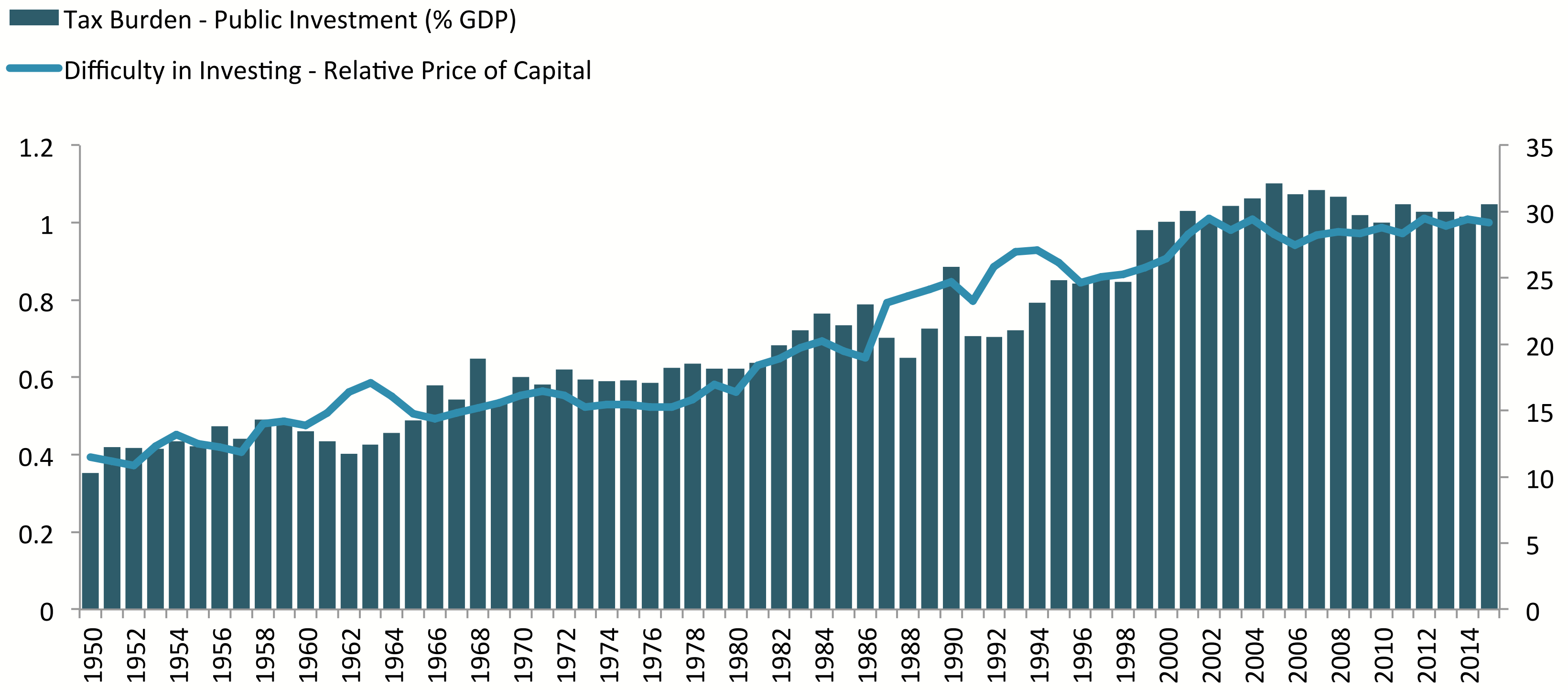
Crowding-in will be a macro force reducing the Brazilian Cost

The distortions in the investment caused by the "Brazilian-Cost", which can be measured as a whole by the cost of capital, are highly correlated with the government crowding-out effect (Tax Burden except Government Investment)

Cost of Capital



Source: Ministry of Finance

Potential GDP (average growth over the next 10 years - 2018 to 2027)

Scenario	GDP (%)
Growth over the last 20 years (1994-2013)	3.3
Demographic and World Growth Effect (China)	-1.0
POTENTIAL GDP WITHOUT REFORMS	**2,3**
Microeconomic reforms	↑
Private Sector Crowding-In	↑

Source: Ministry of Finance

Conclusion

Final Remarks

- **The Government is taking the necessary steps to ensure the stability of the economy. As a result, the economic fundamentals have improved in recent months.**
- **The government is committed to reducing the size of the state in the economy.**
- **Structural reforms will increase productivity and competitiveness.**
- **Regulatory agencies will be strengthened, as well as the management of state-owned enterprises.**
- **The government is committed to promoting a more market friendly environment.**
- **Brazil is building the path to a new cycle of growth, offering opportunities for investment.**

Ministry of Finance

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Henrique Meirelles