Fitch Upgrades Brazil to Investment Grade; IDRs to 'BBB-'

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Fitch Ratings-New York-29 May 2008: Fitch Ratings has upgraded Brazil as follows: --Long-term foreign currency IDR to 'BBB-' from 'BB+'; --Long-term local currency IDR to 'BBB-' from 'BB+'; --Country ceiling to 'BBB' from 'BBB-'; --Short-term IDR to 'F3'. The Rating Outlook is Stable. The rating upgrade reflects the dramatic improvement in Brazil's external and public sector balance sheet that has greatly reduced Brazil's vulnerability to external and exchange rate shocks and entrenched macroeconomic stability and enhanced medium-term growth prospects. The authorities have established a track record of commitment to low inflation and a primary budget surplus that has dispelled previous concerns over medium-term fiscal sustainability. Brazil's investment-grade ratings are also supported by its diverse, high value added economy (reflected in a per capita income, which at approximately US$7,000 is in line with the 'BBB' median), and its relative political and social stability. 'The impressive improvement in external finances, in part due to higher commodity prices but also the result of good policy management, along with the sovereign's net creditor status has made Brazil much more resilient to global financial shocks and enhanced the credibility of its macroeconomic policy framework,' said Shelly Shetty, Senior Director in Fitch's sovereign group. 'A growing consensus across the political spectrum on macroeconomic policies also reduces the potential for a marked departure from the current setting,' Shetty said. Brazil has emerged as a net public external creditor for the first time, thanks to the government's skillful liability management and a significant accumulation of international reserves, that currently stand at nearly US$ 200 billion. Net public external debt reached -34% of CXR in 2007, better than the 'BBB' median of -17% and comparable to that of Peru and Kazakhstan, even though the latter are larger commodity exporters than Brazil. Brazil's policy framework is gaining credibility and the improved structure of public debt has reduced the 'fiscal dominance' of monetary policy decisions by largely eliminating the vulnerability of the public sector's balance sheet to exchange rate shocks, underpinning the credibility of the inflation target and the central bank's policy freedom. The central bank has not hesitated in recently raising policy interest rates in order to fight inflation and to anchor inflation expectations. Moreover, the government continues to demonstrate fiscal discipline by restating its primary surplus target of 3.8% of GDP even after the loss of 1.5% of GDP in revenue as a result of the failure of Congress to renew the CPMF (financial transaction tax) in December 2007. The fiscal results of the first four months of 2008 suggest that the government will comfortably meet its primary surplus target for this year. 'While Brazil's growth continues to lag that of Russia, India and China and low-investment-grade peers, Fitch is more confident that greater macroeconomic stability, reduced external vulnerabilities, higher foreign direct investment and the benefits of past microeconomic reforms will allow higher and more stable growth performance than previously,' said Shetty. Brazil's current growth cycle has been the longest in the last 20 years, and Brazil's recent growth performance has helped it close the gap between its five-year growth average (4.5%) and the 'BBB' median (5%). Formalization of the economy, credit growth and greater certainty on macroeconomic variables (thanks to higher policy discipline) are fuelling consumption and investment in Brazil and should allow the country to grow at a faster pace than in the past. Brazil's ratings continue to be constrained by structural weaknesses in public finances, a heavy government debt burden (67% of GDP versus 28% for the 'BBB' median), an unfavorable, albeit improving structure of domestic debt and a glacial pace of structural reforms. Easing of these constraints through implementation of reforms that unleash the potential of the economy and strengthen public finances would be viewed positively. On the other hand, persistent policy slippage that undermines the credibility of the current policy framework could negatively affect Brazil's ratings. Fitch will hold a teleconference tomorrow at 10 AM ET to further explain the rationale behind the upgrade. Call details to follow. Contact: Contact: Shelly Shetty +1-212-908-0324, Erich Arispe +1-212-908-9165, New

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