# Fitch Sube la Calificación Soberana de Brasil a 'B+', Perspectiva Estable

6 de noviembre de 2003

Fitch Ratings-New York-November 6, 2003: Fitch Ratings today upgrades Brazil's sovereign rating to 'B+' from 'B', reflecting the improving performance of the country's economy as well as its macroeconomic policy framework. Fitch believes that the precautionary agreement with the IMF announced Nov. 5 demonstrates the commitment of the Brazilian authorities to appropriate fiscal policy settings and signals the IMF's intention to help financially insulate Brazil from external shocks over the medium term. The Rating Outlook is Stable. Balance of payments performance in Brazil has improved and should continue to underpin an easing external debt burden. Brazil's trade surplus is likely to exceed US$23 billion this year, up from US$13.1 billion last year, as exports have expanded 20% in the year to end-October. Brazil's diverse export base is reflected in strong growth in exports to China and the European Union and in such products as soy beans, metals and transportation equipment. As a result, Brazil could show a small current account surplus this year of nearly US$3 billion, the first since 1993. A rebound in domestic demand next year will probably push the current account back into deficit. This, combined with external amortizations of US$36.9 billion next year, would result in a high external financing need of 52% of current external receipts, though down from 111% in 1999. Capital inflows have improved, with a rollover rate on medium and long-term debt amortizations of 85% in the year to September, about where Fitch estimates rollover rates need to be to keep foreign exchange reserves stable. The IMF program announced this week would make near-term balance of payments support available (including US$6 billion in new funds) and pushes forward heavy amortization payments due in 2005. Likewise, the program signals the Fund's support of Brazil's macroeconomic policy framework and financial backing in the event of unforeseeable shocks. Monetary policy has been successful in the last year, yielding a reduction in consumer price inflation from a high of 17.2% in May (year-on-year) to 14.0% in October and likely below 10% by year-end. In the process, the monetary authorities have already unwound 750 basis points (bps) of the 850 bps in rate hikes made over the last year. Further rate cuts are likely, given inflation expectations for next year near 6%, which should continue to underpin a rebound in economic activity. Yet recent double-digit private sector wage hikes suggest that backward wage indexation could slow progress on inflation reduction and therefore any future monetary easing. Likewise, such wage settlements could have a fiscal impact if they translate into higher wage pressures in the public sector next year. The Brazilian authorities have agreed to maintain a 4.25% public sector primary surplus target through 2004. Fitch believes that Brazil's high government debt burden and heavy external financing needs warrant a primary surplus of 4.25% of GDP or higher over the medium term. Gross general government debt is expected to end 2003 at 79% of GDP, comparing unfavorably with other speculative grade sovereigns. Higher primary surpluses would increase the likelihood of a virtuous cycle of lower real interest rates, higher GDP growth, a firm exchange rate, and therefore a declining debt-to-GDP ratio, which Fitch believes would be necessary for further improvements in sovereign creditworthiness. Debt management operations this year, which have reduced the sovereign's foreign currency exposure by US$14.4 billion, support sovereign creditworthiness. The portion of U.S. dollar-indexed liabilities fell to 25.5% of total domestic debt by late October from 37% at year-end 2002. An economic environment of slow growth and declining inflation this year has put tax revenues under pressure, with real tax revenues (excluding non-recurring items) up only 1.6% in September 2003 over the year-earlier period, versus an average of 5.7% 3Q03/3Q02 and 16.7% 2Q03/2Q02. Nevertheless, through spending restraint, the authorities have achieved a primary surplus of R$57 billion in September YTD, exceeding the R$54.2 billion target. Yet Brazil's margin above its target has narrowed, and unless economic activity picks up, the authorities could be pressed to produce the requisite primary surpluses next year in an environment of high unemployment (12.9% in September) and expectations of increased social spending under the Lula government. Finally, President Lula remains popular and commands majorities in Congress nearly large enough to pass Constitutional amendments. Fitch expects social security, tax and bankruptcy reforms to pass by early 2004, which, while modest in economic terms, will represent major political victories. Second-stage reforms in revenue earmarking, central bank autonomy, social security, taxation, privatization and regulation would be important for future sovereign credit improvements. Contact: Roger M. Scher, +1-212-908-0240, Morgan C. Harting, +1-212-908-0820, New York or David Riley +44 (0)20 7417 6338, London. Media Relations: Matt Burkhard +1-212-908-0540, New York.