Eleventh Annual International Seminar on Policy Challenges for the Financial Sector

Seeing Both the Forest and the Trees—Supervising Systemic Risk

Session 4: Different strokes for different folks - experience and expectations from macroprudential policy responses

Brazilian Experience with Macroprudential Policy

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BCB Mission

• To ensure the stability of the currency's purchasing power and a solid and efficient financial system

• Inflation targeting
• Floating exchange rate
• Sustainable Fiscal Policy

• Macro and micro prudential regulation
• Solid Supervision

Complementary
Macroprudential policy goals

• Context
  • Limit the risk of system wide financial distress
  • Maintain the provision of financial services
  • Reduce costs for the real economy (output loss)

➢ Effect on aggregate demand (price stability)
How to meet those goals

• Damp the build-up of system wide risk
  • reduce interlinkages
  • sound credit origination
  • inflows volatility

• Build up buffers
  • banks' K requirements
  • reserve requirements
  • foreign reserves

No clear board

• No clear board with traditional monetary and fiscal policy either
Brazilian experience

• Context
  • Brazil sailed well through the crisis
  • Credible macroeconomic framework
  • Well regulated and solid financial system

• Massive inflow of foreign capital
• Strong credit grows
## Capital inflows

### Foreign Capital - Inflows from January to April

<table>
<thead>
<tr>
<th>Selected items</th>
<th>Jan-Apr 10</th>
<th>Jan-Apr 11</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI</td>
<td>7.8</td>
<td>23.0</td>
</tr>
<tr>
<td>Stocks</td>
<td>8.6</td>
<td>1.7</td>
</tr>
<tr>
<td>Fixed income</td>
<td>5.7</td>
<td>-1.2</td>
</tr>
<tr>
<td>Loans (long term)</td>
<td>10.6</td>
<td>17.1</td>
</tr>
<tr>
<td>Loans (short term)</td>
<td>3.0</td>
<td>10.5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>31.9</strong></td>
<td><strong>54.5</strong></td>
</tr>
</tbody>
</table>

Source: BCB
Reasons for strong capital inflows

• **Structural**
  • Solid macroeconomic fundamentals
  • Sustainable macroeconomic policy framework
  • A growing middle class (potential new consumers)

• **Temporary**
  • Ample liquidity in international financial markets
  • Rising interest rates (to fight inflation)
Macroprudential Measures

• Established unremunerated reserve requirement on short FX positions exceeding either US$3 billion or the bank’s regulatory capital (Jan 2010)

• Increase in financial transactions tax on certain inflows
  • Non resident fixed income investments: (raised to 6%)
  • Short-term external loans or debt issues

• Foreign reserves increase to US$ 330 billion from US$ 186 billion (2008)
Credit / GDP

Source: BCB

*March 2011
Real Interest Rate

Sources: BM&FBovespa / BCB

Market Rate 360 days and IPCA expected 12 months (Focus)

Apr 11 6.7%
Credit: Provisions vs. Non Performing Loans

Source: BCB
Household Indebtedness

Source: BCB

% monthly income

Debt
Debt Service

Jul 06  Jan 07  Jul 07  Jan 08  Jul 08  Jan 09  Jul 09  Jan 10  Jul 10  Jan 11
Increasing capital requirement for fast-growing lines of credit

- Increased capital requirements for consumer loan exposures involving longer maturities and higher LTVs. The risk weight for such exposures was increased from 100 to 150%.

<table>
<thead>
<tr>
<th>Operation</th>
<th>Maturity and LTV</th>
<th>Capital requirement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vehicles (financing and leasing)</td>
<td>between 24 and 36 months and LTV &gt; 80%</td>
<td>16.5%</td>
</tr>
<tr>
<td></td>
<td>between 36 and 48 months and LTV &gt; 70%</td>
<td></td>
</tr>
<tr>
<td></td>
<td>between 48 and 60 months and LTV &gt; 60%</td>
<td></td>
</tr>
<tr>
<td></td>
<td>more than 60 months and any LTV</td>
<td></td>
</tr>
<tr>
<td>Payroll deduction loans</td>
<td>more than 36 months</td>
<td></td>
</tr>
<tr>
<td>Personal loans</td>
<td>more than 24 months</td>
<td></td>
</tr>
<tr>
<td>Other consumer loans</td>
<td></td>
<td>11%*</td>
</tr>
</tbody>
</table>

*Unchanged
Macroprudential Measures

• Minimum payment for credit card bill
  – 15% (effective Jun 2011)
  – 20% (effective Dec 2011)

• Increased bank reserve requirements on demand and time deposits (Feb, Jun, Dec 2010)
  - From R$ 170 billion (2008) to R$ 400 billion
  - Important source of liquidity during the crisis
## Immediate effects of the measure

<table>
<thead>
<tr>
<th></th>
<th>Maturity (months)</th>
<th>Interest rate (% per year)</th>
<th>New Loans (R$ million/day)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Before</td>
<td>After</td>
<td>Before</td>
</tr>
<tr>
<td>Vehicles</td>
<td>43</td>
<td>36</td>
<td>23.1</td>
</tr>
<tr>
<td>Personal credit (^{(1)})</td>
<td>56</td>
<td>45</td>
<td>42.8</td>
</tr>
<tr>
<td>Payroll-deducted loan (^{(2)})</td>
<td>58</td>
<td>54</td>
<td></td>
</tr>
</tbody>
</table>

(1) In 'maturity', data does not include payroll-deducted loan

(2) Data includes only civil servants and social security beneficiaries (INSS)

Source: BCB
New Loans: Vehicles

Source: BCB