Non Resident Investors in Brazilian Public Debt

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The importance of Non Resident Investors

Overview

- Since the 90s, the domestic market for public bonds have grown substantially in the emerging economies.

- Growth led by:
  - Favorable international environment until the middle of 2008
  - Great liquidity
  - Better macroeconomic fundamentals, in general
  - Change in technology - real time trades, instant data streamers
  - Concern on excess of volatility

- Brazil experienced the same, with an increase in the stock of the domestic public debt and, on the other hand, a reduction in the external debt.
Withholding tax exemption for Non Resident Investors – Feb-06

On Feb-06, the gov’t launched a measure that exempted non resident investors from taxes and then converted it in a law afterwards.

Foreign Investors: Domestic Debt Participation %

- Law 11,312/06 Tax Exemption
- IOF tax exemption
- IOF shift to 4%
- IOF shift to 6%
- 2% IOF tax on NRI

Source: Until 06/2008 CVM. After, SELIC (Central Bank).
NRI in the domestic market

Non-resident share in Overall Federal Public Debt

Source: National Treasury
Size matters

Size of the domestic markets for public bonds - BRA - 8th largest

Market development
Liquidity and market depth
Sophisticated investors

Source: BIS Quarterly Review, December 2008
Brazil has changed its base of investors

- The Brazilian debt profile has changed significantly along the years: larger participation of investors with a long term profile.

**Investors Base - Aug-10**
- Banks: 37.8%
- Funds: 29.7%
- Pension Funds: 16.6%
- Foreign Investors: 10.1%
- Insurance: 3.9%
- Others: 2.0%

**Investors Base - Jan-07**
- Banks: 41.4%
- Funds: 35.9%
- Pension Funds: 17.6%
- Foreign Investors: 0.9%
- Others: 4.2%

Source: National Treasury
The non resident investor has a distinct profile. Among its features, we find:

- Demand for fixed rate bonds;
- Longer term portfolio;
- More appetite for duration.

The two first features contribute, respectively, for the following objectives of the Brazilian public debt management:

- Increase of the fixed rate share;
- Lengthening of the maturity profile of the debt.
The non resident investor has a preference for fixed rate bonds, and, to a lesser extent, inflation linked bonds.

The participation of non resident investors in fixed rate bonds has grown strongly, in line with the Treasury strategy to increase the participation of the fixed rate debt and to reduce participation of the floating rate debt.

Note: For Aug-10, NRI share on IP and fixed rate bonds are 4% and 23.6% respectively.

Source: National Treasury
The IOF tax policy

- It’s a regulatory tax:
  - Has been changed a number of times since the tax exemption;
  - Negatively affects the benchmark investment indexes overseas;

- The world is going through a extraordinary period
  - Search for high yields
  - Successful stories
  - Dangers of overshooted FX-rate
Contact

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