TESOURO NACIONAL

How Have Debt Managers Increased the Attractiveness of Local Currency Debt

Sovereign Debt Management Forum

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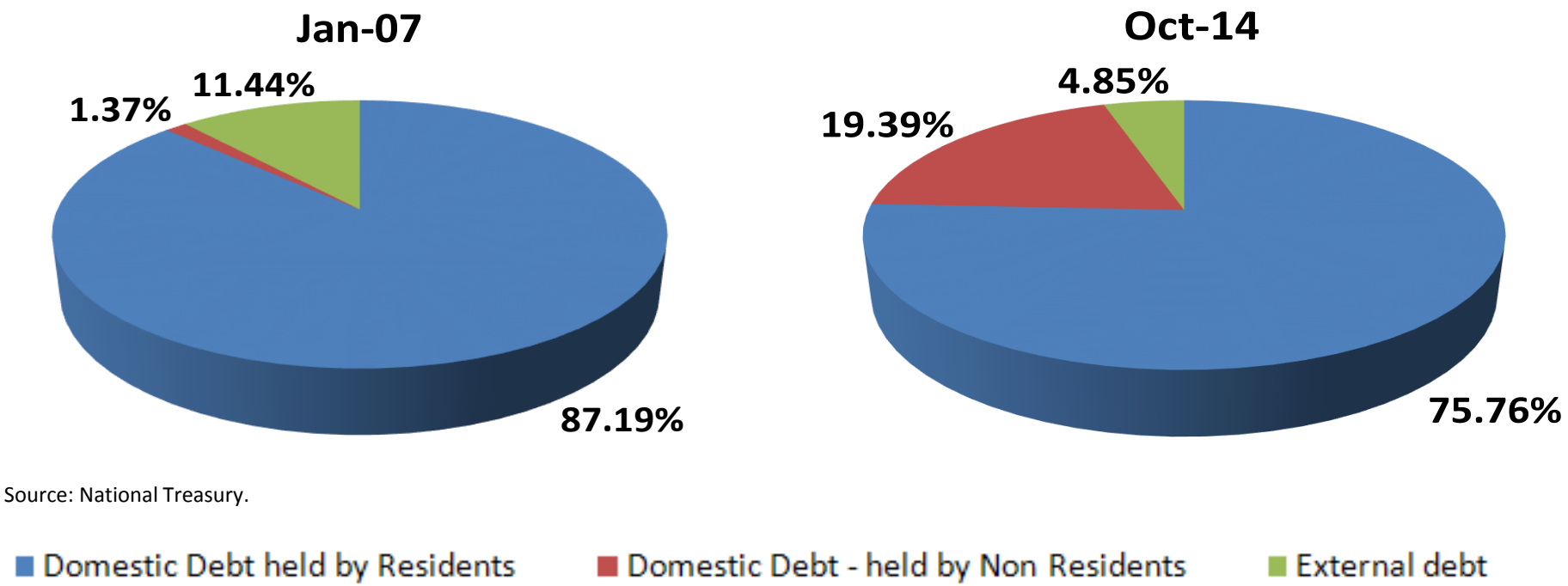
Non-Resident Share in Federal Public Debt (FPD) held by the market

Recent Evolution (as % of FPD)



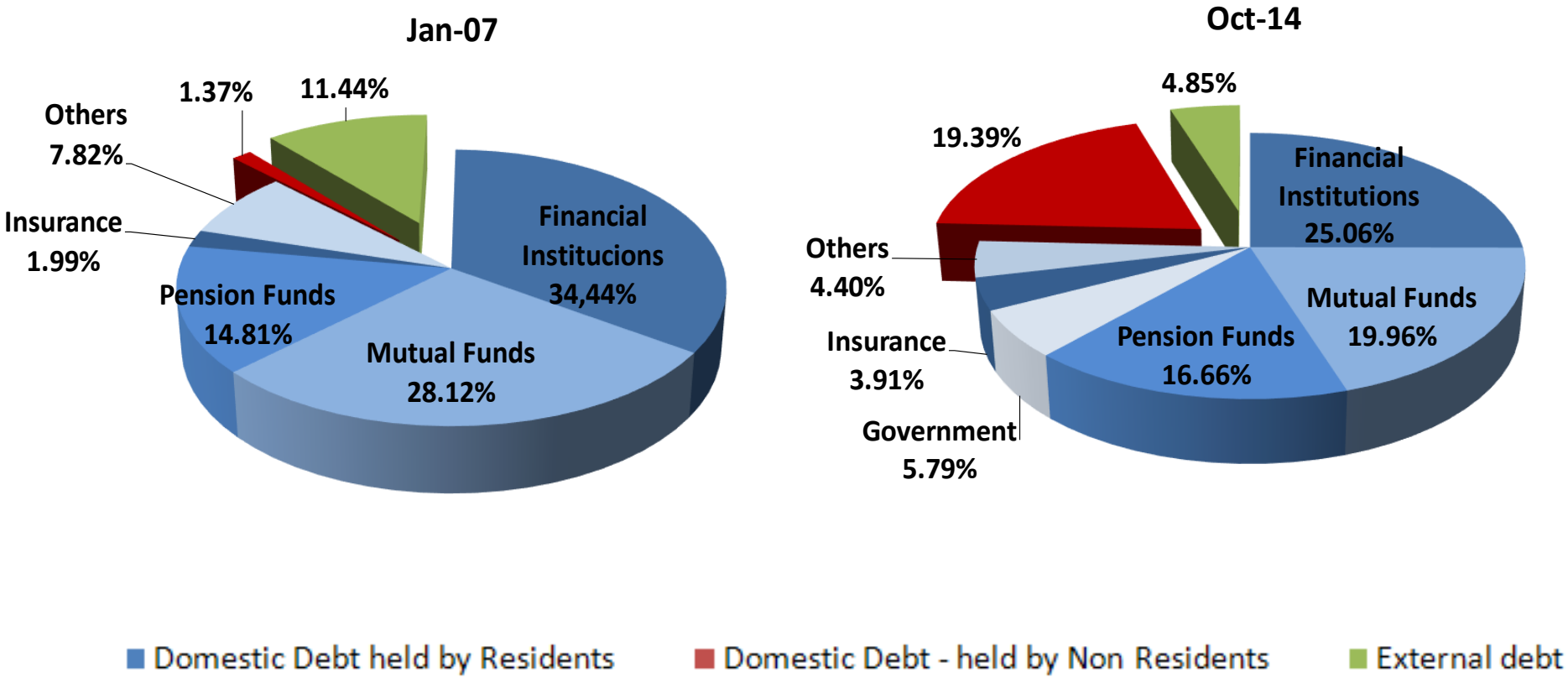
Source: National Treasury.

» Non resident participation in Brazilian domestic debt is lower than the observed in some EM countries. However, in nominal terms, the amount is among the most representatives: USD 167 billion (BRL 418 billion).

» Since 2007, non resident net purchase of Brazilian domestic bonds accumulated more than USD 100 billion, similar to Mexico, , and much higher than the third place, South Africa, with USD 50 billion.

Federal Public Debt (FPD) Composition - Holders

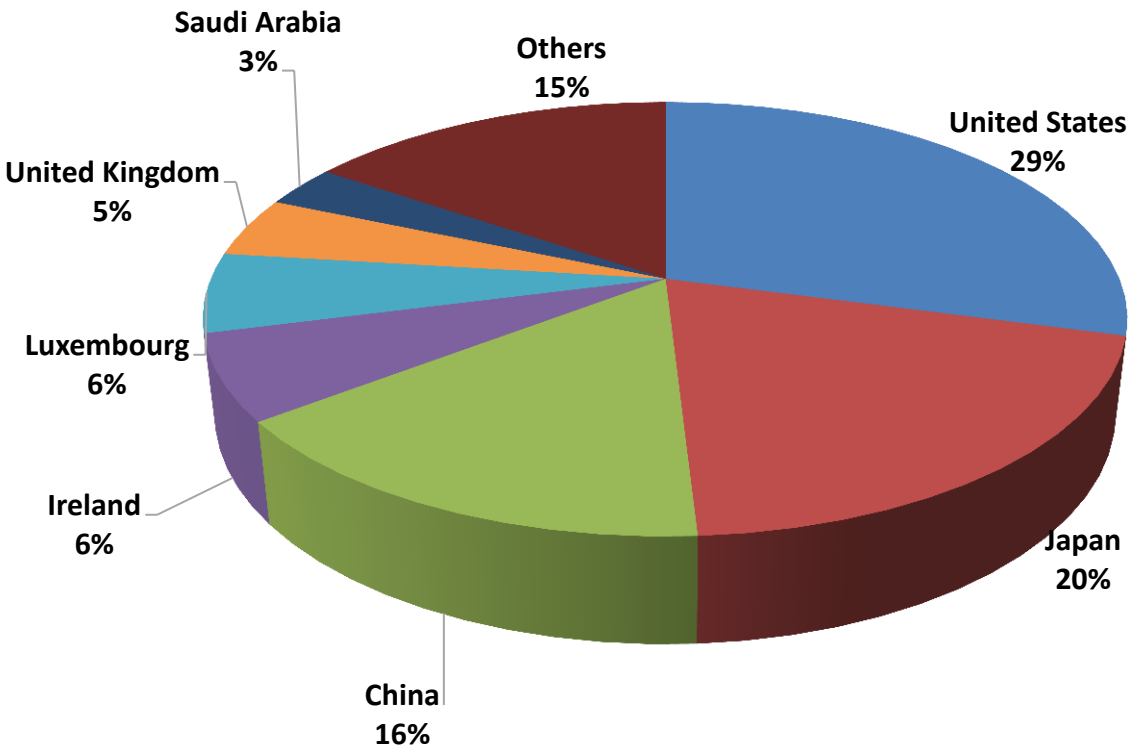
Recent Evolution (as % of FPD)



Source: National Treasury.

Domestic Federal Public Debt (DFPD)

Non-Resident Investors in Fixed Income, by Origin – Jun/14



Source: National Treasury, based on custodian´s data.

Increasing Attractiveness: moving debt credit rating to investment grade

Recent Evolution of Brazil's Credit Rating

	Speculative Grade																		Investment Grade		Outlook
S&P	D	...	2004	BB-	2006	BB	2007	BB+	2008	BBB-	2011	BBB	2014	BBB-		...		AAA			(stable)
Fitch	D	...	2004	BB-	2006	BB	2007	BB+	2008	BBB-	2011	BBB		BBB+		...		AAA			(stable)
Moody's	C	...	2005	Ba3	2006	Ba2	2007	Ba1	2009	Baa3	2011	Baa2		Baa1		...		Aaa			(negative)
DBRS	D	...		BBL		BB	2007	BBH	2008	BBBL	2011	BBB		BBBH		...		AAA			(stable)
JCR	D	...		BB-		BB		BB+	2008	BBB-	2011	BBB		BBB+		...		AAA			(stable)
R&I	D	...	2004	BB-	2006	BB	2006	BB+	2007	BBB-	2011	BBB		BBB+		...		AAA			(stable)

Source: Rating Agencies

- » Macroeconomic stability, reflected in ratings, attracted a new group of non resident investors for the domestic debt
  - » Primary surplus of 3% of GDP per year from 2000 to 2008:
    - » Net debt to GDP reduced from 50% of GDP in 2005 to 35% in 2014. Gross debt was kept stable in 60% of GDP during the period (accumulation of assets - international reserves and loans to public banks - to face the crisis);
  - » Inflation within the target limits since 2004
  - » Central Bank reserves enough to pay overall country external debt and five times bigger than public external debt

Increasing Attractiveness: Transparency and Communication

Release of documents and Investor Relations Office

Communication

» Investor Relations Office: created in 2001, within the Debt Management Office, to deal with investors, rating agencies and press, among other stakeholders

» Regular road shows and teleconferences with investors

Transparency

» Accountability: Monthly and Annual Debt Reports => Backward looking

» Annual Borrowing Plan => Forward Looking

- » Objectives, guidelines and strategies for domestic and external debts
- » Optimal debt compositions released, with quantitative targets
- » Debt indicators upper and lower limits for the year end: stock, composition (fixed, inflation linked, floating and exchange rate), average maturity and % of debt outstanding in 12 months

Increasing Attractiveness: Transparency and Communication

Release of documents and Investor Relations Office

Transparency

» Annual Auctions Schedule: investors acknowledge and understand how the Treasury operates in the market

Frequency of auctions to be held by the National Treasury in 2014

Bond	Tradicional		Exchange		Buyback	
	Periodicity	Auction Format*	Periodicity	Auction Format	Periodocity	Auction Format
LTN	Weekly	Discriminatory				
NTN-F	Fortnightly	Discriminatory			Monthly	Discriminatory
LFT	Monthly	Discriminatory				
NTN-B	Fortnightly	Uniform	Monthly	Discriminatory	Fortnightly	Discriminatory

* Criterion for selecting proposals in the auctions: in the discriminatory auction, the proposals accepted pay the price presented in the bid. In the uniform format, all proposals with quotes equal to or greater than the minimum quote will be accepted. This will be applied to all winning proposals.

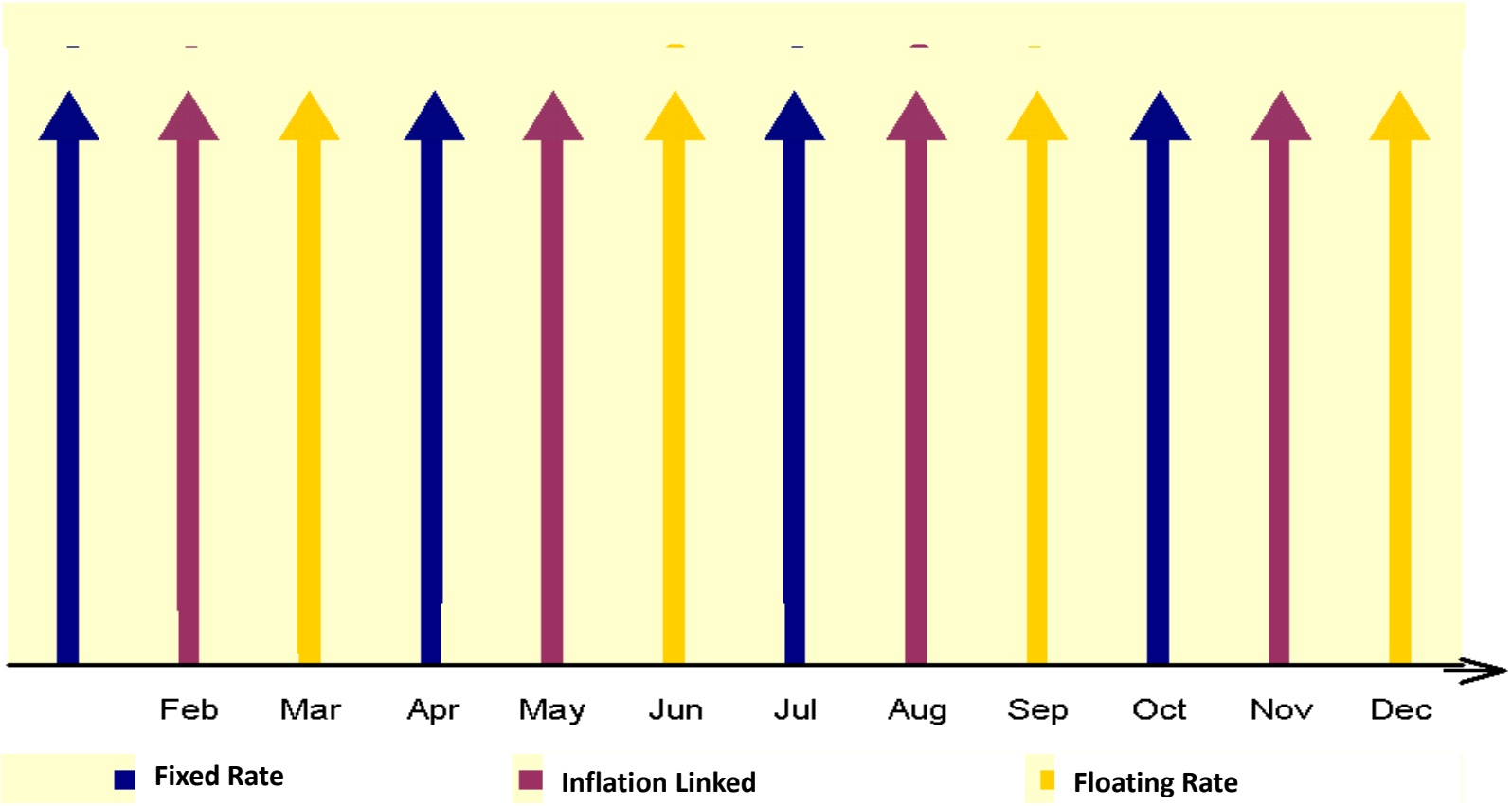
Official annual and quarterly schedules will be released through the site: https://www.tesouro.fazenda.gov.br/en/federal-public-debt/auctions-results.

The government bond auctions adopted by the Treasury have the following specific purposes:

- Traditional Auctions: have the main purpose of refinancing the Federal Public Debt through issuances of fixed rate, floating rate and inflation-linked government bonds;
- Exchange Auctions: consist of exchanges of shorter-term securities for longer-term securities, with the objective of lengthening or improving the debt profile; and
- Buyback Auctions: ensure liquidity to the bondholder.

Increasing Attractiveness

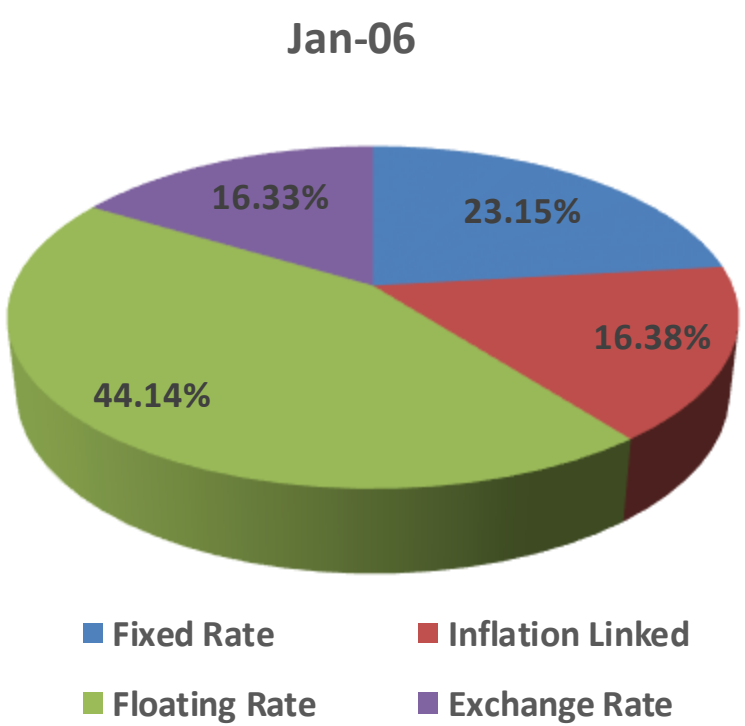
Benchmarks for bonds regularly auctioned

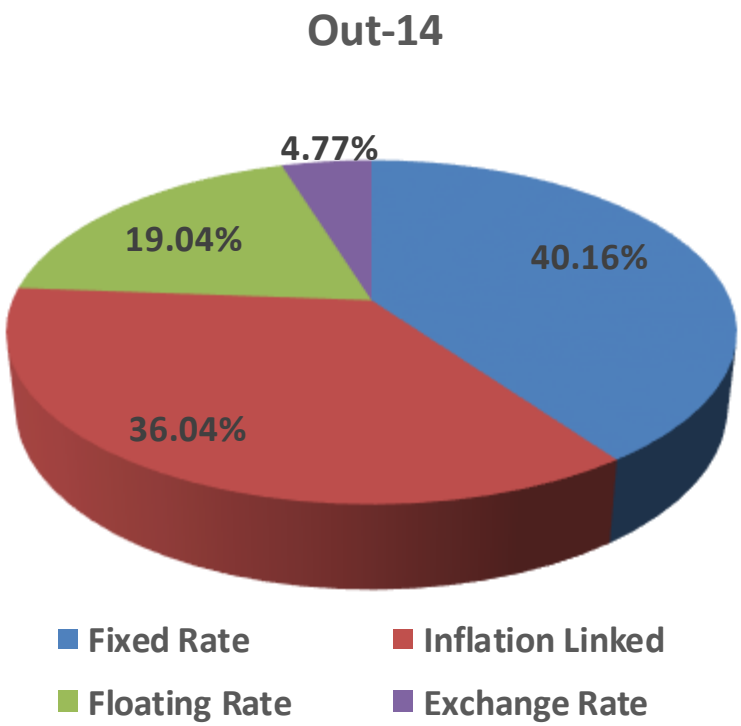


Source: National Treasury

Increasing attractiveness through enhancing Public Debt Composition

Replacement of floating-rate securities by fixed-rate and inflation-linked bonds



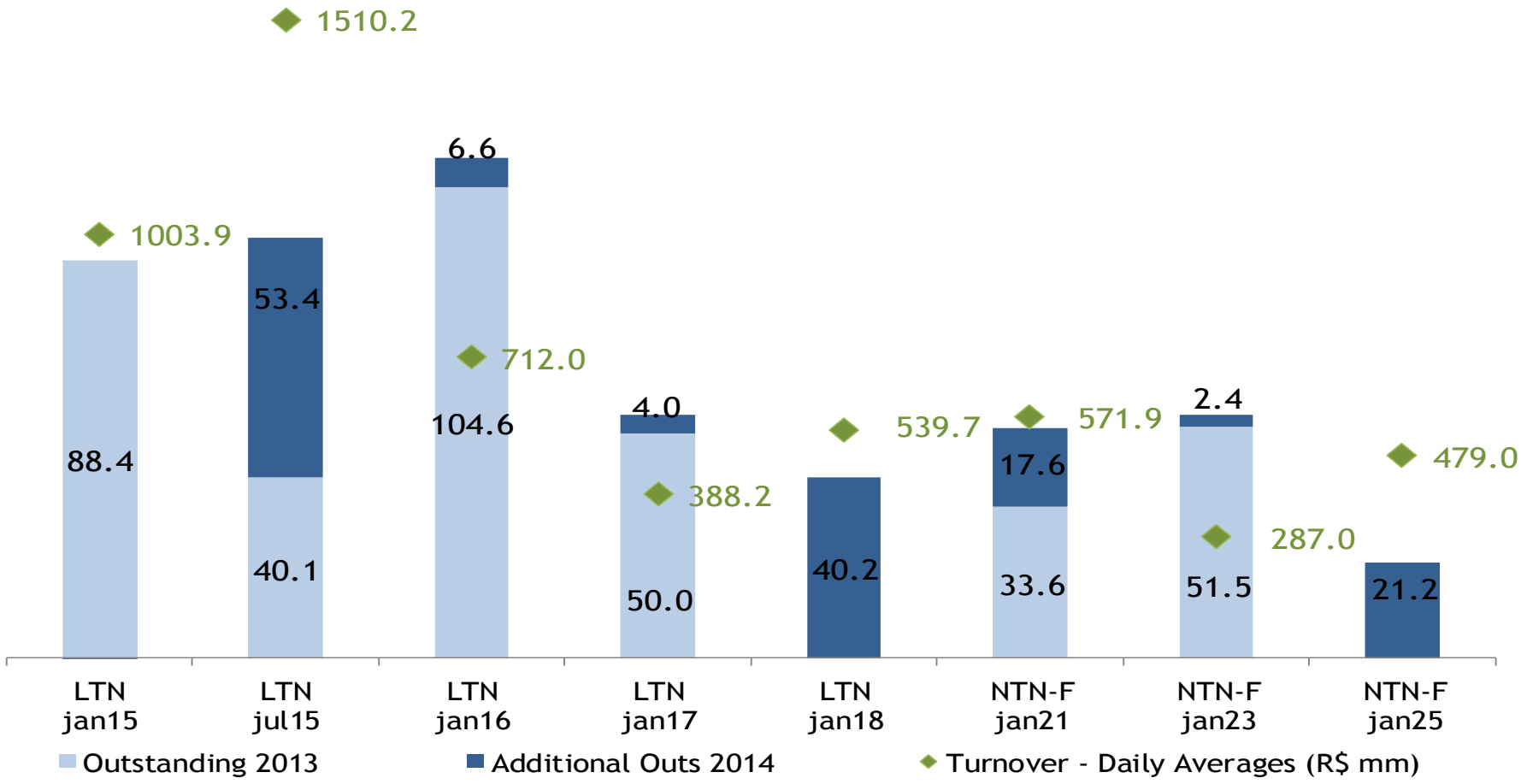


Source: National Treasury.

Note: Federal Public Debt, which includes both domestic and external liabilities.

Increasing Attractiveness: Liquidity Matters

Domestic Fixed Rate Bonds: Outstanding (R$ bn) and Secondary Market Turnover (R$ mm) – Sep 2014



Source: National Treasury and Central Bank

Annex

Measures to enhance attractiveness for Non-Resident Investors

Search for high yields: is it enough?

» **Removal of withholding tax for foreigner investors – Feb/06**

» **Cutting the Red Tape =>** Unification of registration processes in the regulatory authorities: Central Bank, CVM (Brazilian SEC) and RFB (Brazilian IRS)

- » RFB and CVM create a register number in 24h
- » In general, a single institution provides all services the non-resident investor needs no start its operation in the Country: Custodian, Broker, Foreign Exchange Bank and Local representative.
- » Settle an account on the Clearing System (Selic)
- » Dealership System

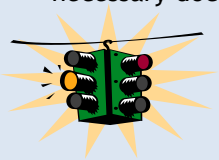
» **No amount limits for non-resident investors in treasury auctions or groups of bonds**

» **No more than 36 hours for a first time non-resident investor to be registered in Brazil. After that, operations can be done in less than one day**

»**Fixed Income ETF – forthcoming**

» **Liquid FX derivatives market - hedging**

Step 1: Bank makes application with necessary documents



Step 2: CVM checks and, upon approval, sends application to RFB (IRS)

Step 3: Automated (electronic) procedure at RFB (IRS) provides CNPJ

Step 4: Ready to go

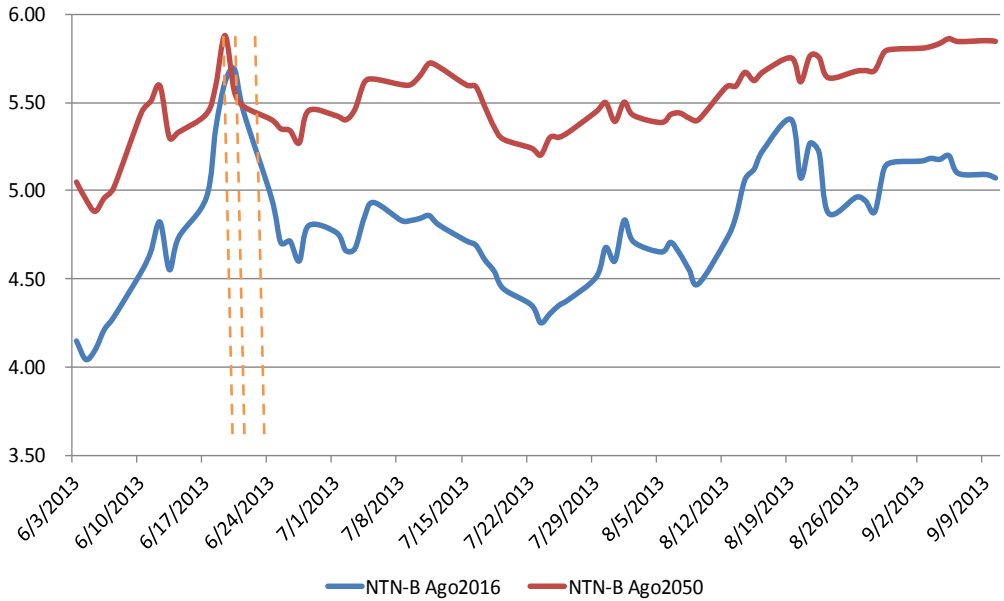
Measures to enhance attractiveness for Non-Resident Investors

What to do in times of crisis?

- **Simultaneous Buy&Sell Auctions in moments of increased volatility => provide price parameters and liquidity:**
  - **May-06** (NTN-B – Inflation-linked bonds)
  - **Oct-08** (NTN-F – Fixed Rate bonds)
  - **Jun-13** (LTN, NTN-F, NTN-B) and **Oct-13** (NTN-B) – Fixed and Inflation-linked bonds
  - **Fev-14** (LTN, NTN-F) – Fixed Rate bonds

2013 Simultaneous Auctions – fixed rate securities

2013 Simultaneous Auctions – inflation-linked securities



Measures to enhance attractiveness for Non-Resident Investors

What to do in times of crisis?

» **Liquidity Cushion => reduces refinancing risk, avoiding the need for financing in less favorable conditions and opening space for buyback auctions to reestablish bonds price equilibrium**

» Domestic: resources in local currency deposited in the Central Bank single account exclusively to pay at least the following three months of debt service (principal and interest)

» External: dollars bought in advance to pay external debt service (principal and interest). The Monetary Council authorizes the Treasury to buy up to 4 years ahead, but we usually buy enough hard currency to pay between one and two years of debt service

» **Futures FX market is highly deep and liquid**