Belo Horizonte, Minas Gerais, Brazil

2019

Annual Borrowing Plan

TesouroNacional

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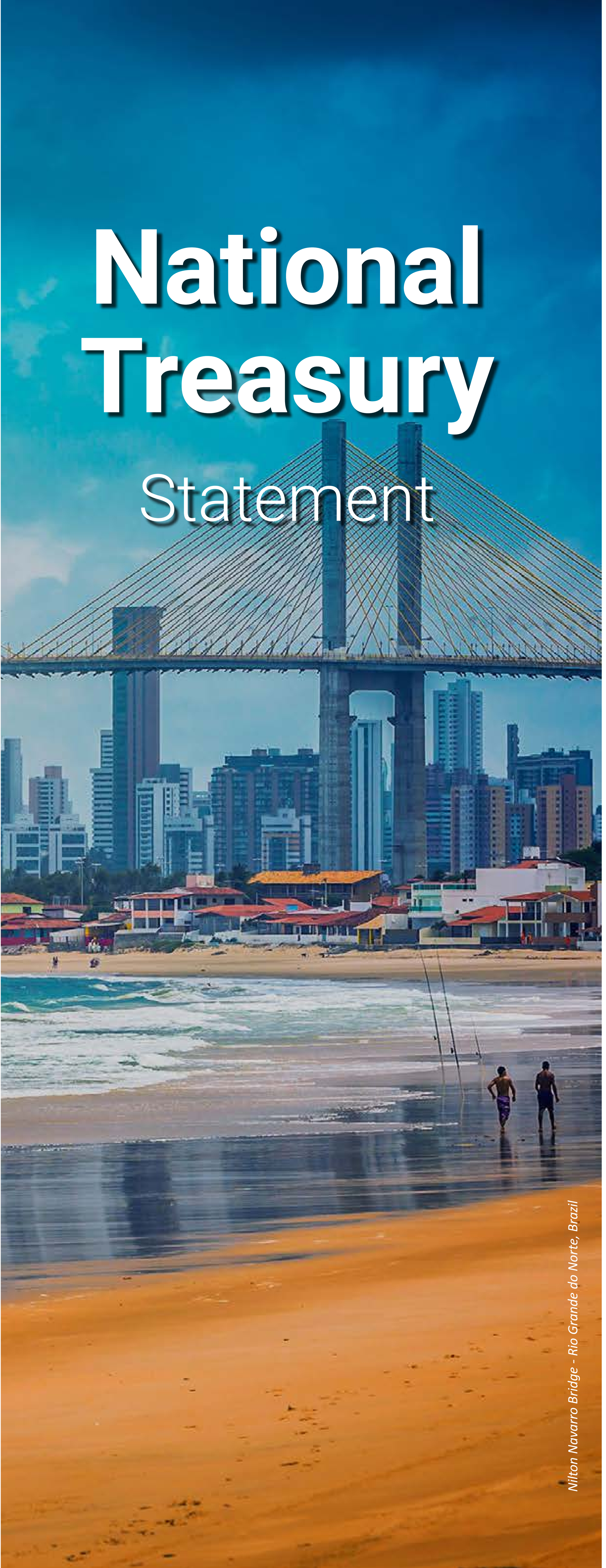
Summary

National Treasury

Statement



The *2019 Annual Borrowing Plan* is a part of the Federal Public Debt (FPD) financing strategy, which includes the guidelines and parameters for the debt management throughout the year. This publication is adherent to the efforts of the National Treasury to communicate with society, promoting transparency and fiscal responsibility culture.

This year the Federal Government will give an additional step towards fiscal consolidation. There are many challenges and the path to be followed requires society's understanding about the importance of balancing the State functions and its ability to keep sound public accounts, ensuring a sustainable public debt path.

The *2019 Annual Borrowing Plan* fulfills the role of reducing uncertainties regarding public debt management and possible implications for the decision-making of the different economic agents. The financing strategy aims to reduce the Federal Public Debt costs in the long term while simultaneously ensuring prudent levels of risk. For this purpose, a well-diversified debt portfolio is sought, preferably with a higher proportion of long-term fixed-rate and inflation-linked bonds, though the balance between costs and risks might admit a significant share of floating-rate bonds on the short term.

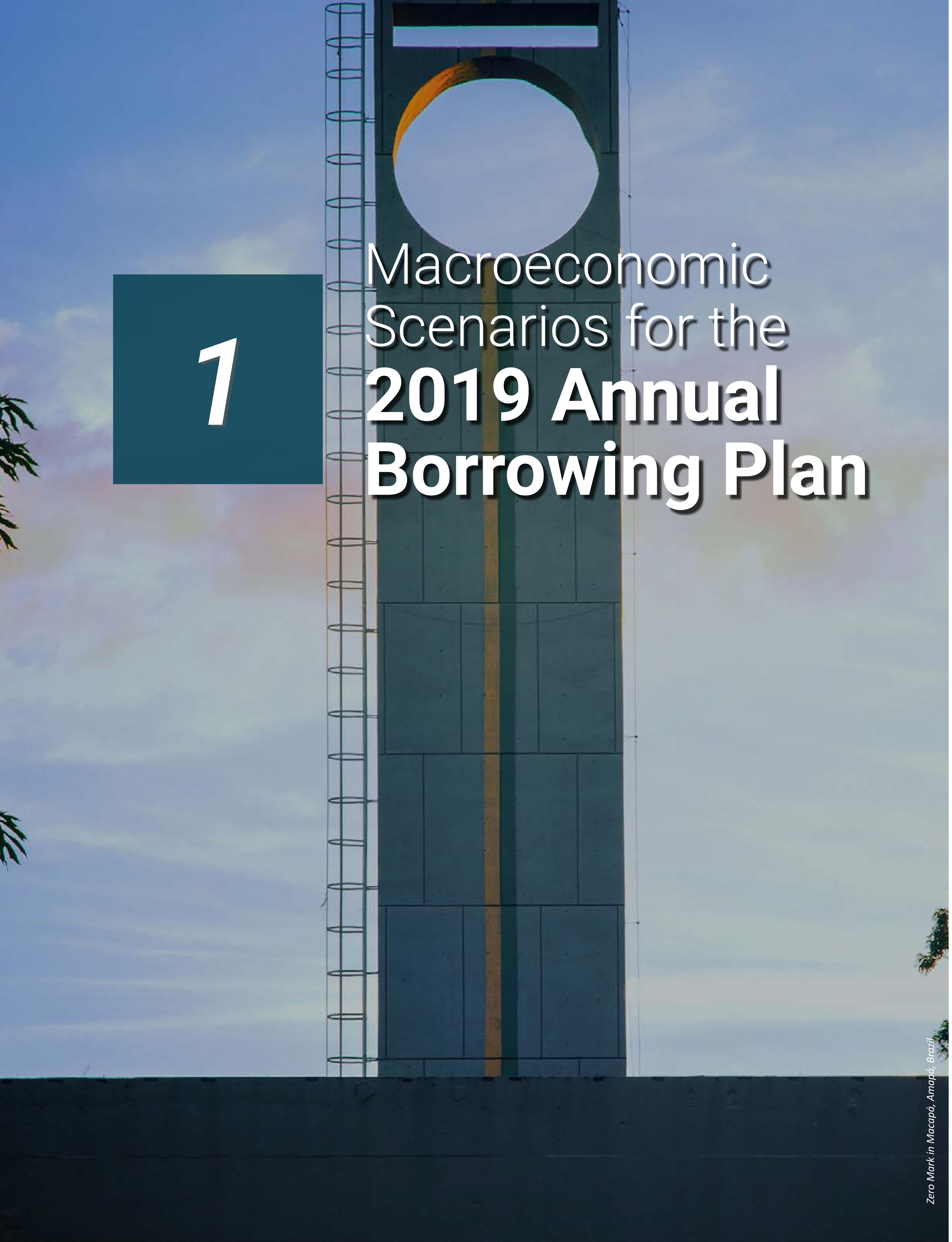
Thus, the planning for 2019 holds the possibility of issuing a higher share of fixed-rate and, to a lesser degree, of inflation-linked bonds compared to the previous year. However, outstanding Federal Public Debt statistics point to a continuation of the trend observed since 2015, which has brought a higher proportion of LFT, relative to other instruments. LFT bonds have risen in the context of fiscal deficits, being attractive to investors at moments of risk aversion, allowing the National Treasury to avoid excessive risk premiums that emerge in such a context. Additionally, LFT help to avoid the concentration of maturities in the short term, figuring as an alternative to fixed-rate bonds with shorter maturities.

Federal debt management objectives and guidelines

On the medium-term perspective, the progress of the reforms agenda is essential to recover fiscal balance and, consequently, to improve the overall Brazilian economic conditions. This outlook will favor federal debt dynamics, allowing it to resume the improvement of composition and maturity profile towards the long-term management guidelines.

In this context the following pages present the *2019 Annual Borrowing Plan*, a publication aimed at reinforcing to our stakeholders the National Treasury commitment with transparency, fiscal responsibility and excellence.

The National Treasury Team


Zero Mark in Macapá, Amapá, Brazil

1 Macroeconomic Scenarios for the **2019 Annual Borrowing Plan**

The global macroeconomic context is marked by the continuity of uncertainties over monetary policy normalization in advanced economies and the possibility of geopolitical tensions. Regarding the baseline domestic scenario, the *Annual Borrowing Plan* assumes the permanence of the economic activity recovery started in 2017 as well as controlled inflation and the ongoing fiscal consolidation. Advancing in the structural reforms agenda is a key factor to consolidate basic conditions for a sustainable economic growth.

> *Challenging and volatile external environment. Nevertheless, domestic scene is dominant, especially regarding the developments on structural reforms and fiscal consolidation.*

In the international scene, uncertainties surrounding the international trade and the slowdown in global economic activity prevail. Tensions over US-China trade war keep bringing volatility to markets while uncertainty mounts over a sharper slowdown in China and in countries highly exposed to the latter. Fiscal developments in Europe and the Brexit are additional risk factors.

The baseline domestic scenario is close to market expectations for 2019 and assumes a new growth cycle sustained by the ongoing economic recovery's consolidation. Inflation under control and target-adherent is central, together with labor market and confidence indicators gradual recovery. An important assumption underpinning this scenario is the promotion of structural reforms, including those aimed at boosting efficiency in the economy. Lastly, the favorable balance of payments funding conditions will remain, with low current account deficit, strong foreign direct investment and robust international reserves level.

To allow some degree of freedom on the debt financing strategy, the *Annual Borrowing Plan* provides alternative scenarios that define reference ranges for the federal debt outstanding, composition and maturity structure at the end of the year. However, these scenarios do not include tail distribution shocks nor stress situations.

In the conservative scenario, the *Annual Borrowing Plan* assumes that the progress on the reform agenda and the economic recovery will be slower, resulting in greater economic uncertainty. Other way around, a more favorable scenario considers a quick fiscal consolidation, grounded on the approval of structural reforms aimed at tackling the primary deficit and bringing gross debt-to-GDP ratio to a declining trajectory in the medium term. Consequently, there would be an increase in perceived predictability and the recovery of confidence, with incentive to consumption and investment, accelerating economic recovery.

Sérgio Motta Bridge, Cuiabá, Mato Grosso, Brazil

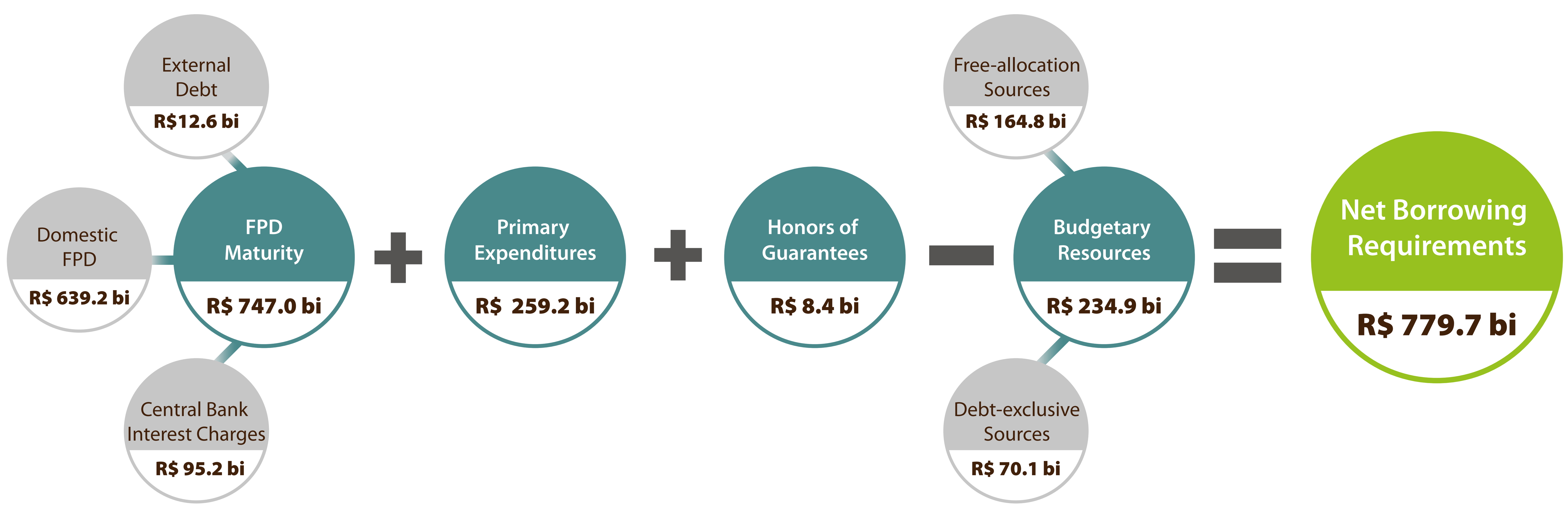
Campo Grande, Mato Grosso do Sul, Brazil

2 Borrowing Requirements

> *The Borrowing Plan covers the federal public debt in the market, which comprises the sum of domestic bonds and external debt, the latter including both bonds and loans.*

The estimate for 2019 federal government gross borrowing requirements reaches BRL 1,014.6 billion, while the net needs amounts to BRL 779.7 billion, as shown in Figure 1.

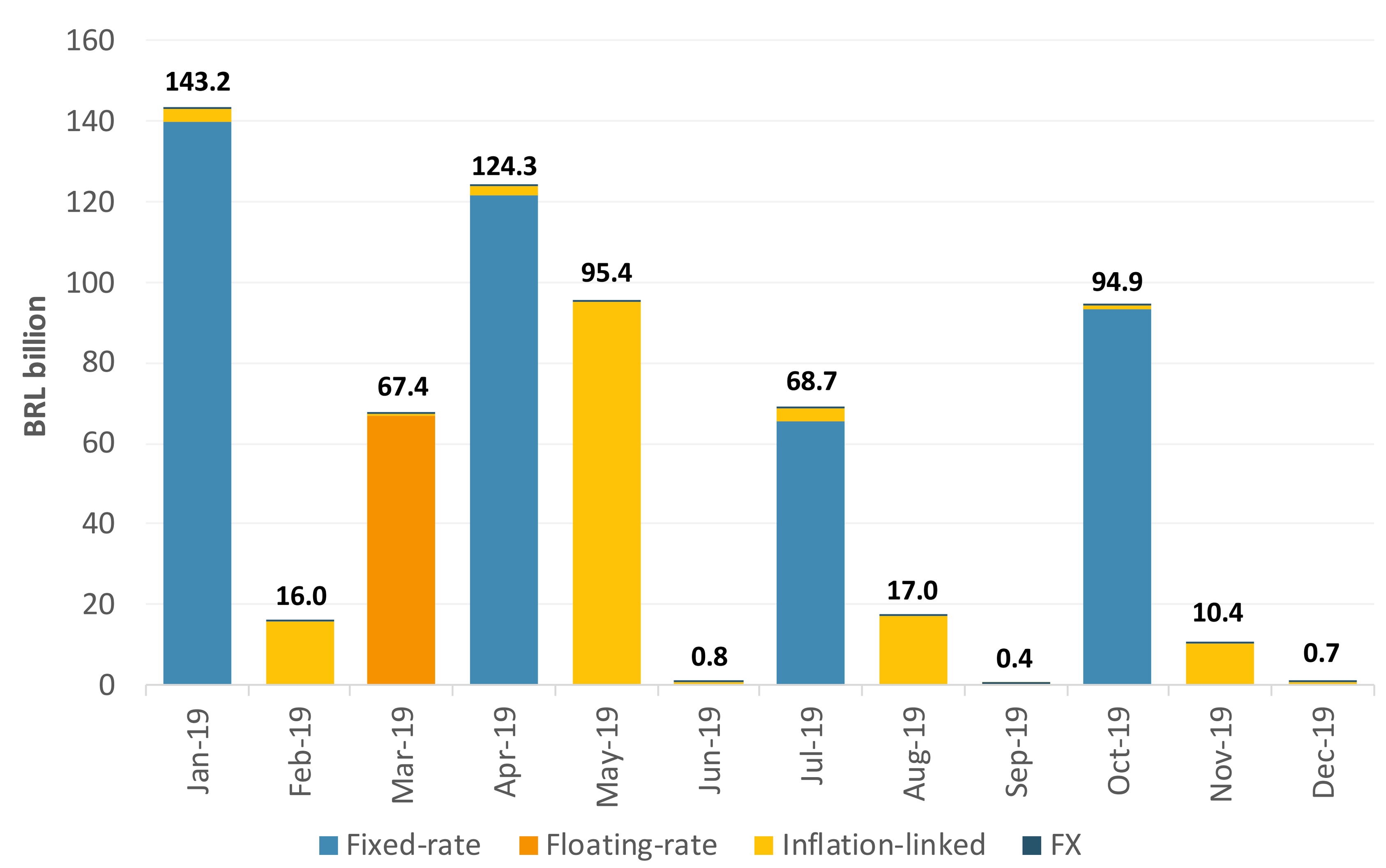
*Figure 1 – **Borrowing requirements in 2019***



***Source:** 2019 Annual Budget Law Draft and National Treasury. Estimated values, as of 12/31/2018.*

Outstanding federal debt maturing in 2019 sums BRL 747.0 billion, including of domestic and external debt maturities, as well as the interest payments relative to the portfolio held by the Central Bank, which by law cannot be rolled over[2]. Domestic federal debt maturities in the bond market amounts to BRL 639.1 billion, of which BRL 473.1 billion in principal and BRL 166.0 billion referring to interest charges. Approximately 70% of these maturities are concentrated in the first half of the year. Fixed-rate bonds mature at the first day of each quarter, while the inflation-linked bonds are distributed in the second month of each quarter, with a highlight in May, which, due to the odd year, has the amortization of the principal of a NTN B. Lastly, the floating-rate bonds feature small magnitude maturity in 2019, reaching BRL 67.4 billion (of which BRL 67.0 billion of LFT) .

*Figure 2 – **Domestic federal debt maturity in 2019***



Source: *National Treasury. Estimated values, as of 12/31/2018.*

[2] According to paragraph 2, article 39, of the Fiscal Responsibility Law, the Central Bank may only buy bonds issued by the National Treasury to roll over the principal of the bonds maturing in its portfolio.

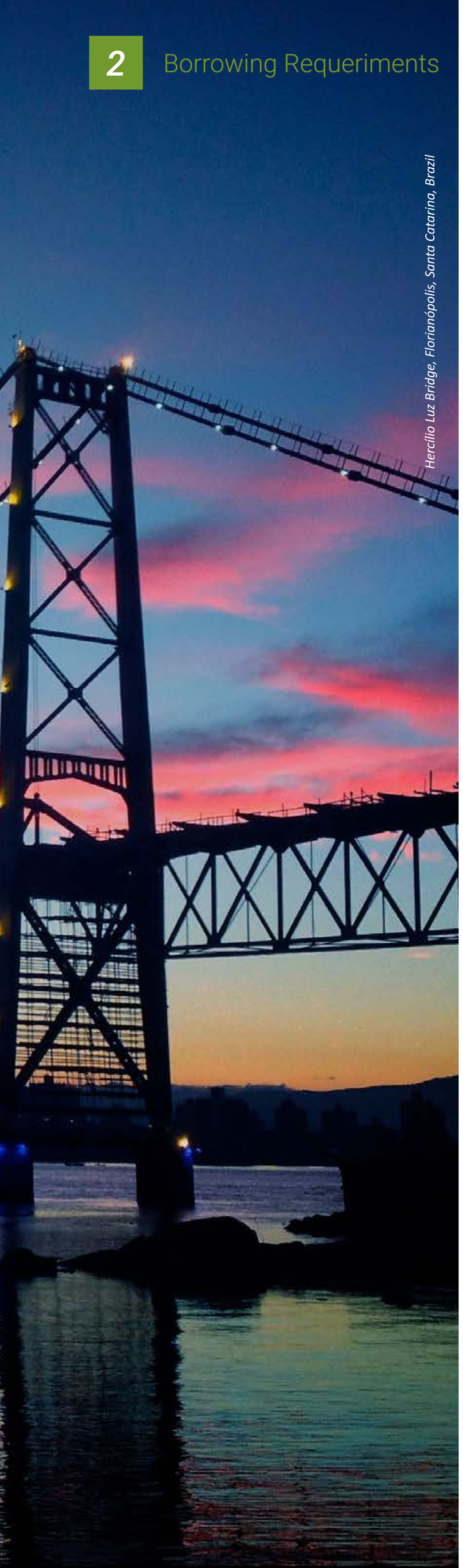
In addition to debt maturities, there is a forecast of using bonds issuances resources for the payment of primary expenditures of the Union's budget, in the amount of BRL 259.2 billion, most of which are intended to cover social security spending (Table 1). However, BRL 258.2 billion are expenses conditioned to the approval of additional credits to the 2019 Annual Budget Law, by absolute majority of the National Congress. This is a requirement for the compatibility between the volumes of borrowing operations and of capital expenditures included in the budget law, in compliance with item III, article 167 of the Federal Constitution (Golden Rule).

*Table 1 – **Government bonds issuances to the payment of primary expenditures (BRL billion)***

2019 Annual Budget Law Draft	Forecasted	Conditioned
Urban Social Security	201.7	201.7
Assistance Benefits (BPC)	30.0	30.0
Compensation to Social Security Fund (FRGPS)	2.5	2.5
Subsidies and Grants	9.3	9.0
Other Current Expenditures	15.7	15.0
Bolsa Família	15.0	15.0
Other	0.7	0.0
Total	**259.2**	**258.2**

Source: *2019 Annual Budget Law Draft and National Treasury*

The gross requirements are complemented by the forecast of honors of guarantees referring to the payment flows in contracts of subnational governments defaulting on debts guaranteed by the federal government, which have adhered or may accede



Hercílio Luz Bridge, Florianópolis, Santa Catarina, Brazil

to the Fiscal Recovery Regime (Complementary Law nº 159, of 2017), provided that the obligations were contracted prior to the approval of the application to the regime (article 17 of the mentioned law).

The 2019 budget foresees the allocation of BRL 234.9 billion in budgetary sources to pay debt maturities, not including bonds issuances and cash availability from previous years. This amount includes resources earmarked to federal debt payments, such as the service of federal government loans to BNDES and to subnational governments, as well as free-allocation sources, to which there is no specific linkage. Deducting these budgetary resources from the gross borrowing requirements, the net borrowing requirements reaches BRL 779.7 billion.

The assignment of free-allocation budgetary sources to the payment of federal debt maturities directly reduces borrowing needs and mitigates the impact on the liquidity reserve (“liquidity cushion”) concerning the use of bonds issuances resources to pay primary expenditures. In practice, the difference between the proceeds from issuing bonds for primary expenditures payments (BRL 259.2 billion) and the free-allocation sources expected for federal debt (BRL 164.7 billion) would be a proxy for the partial coverage of the primary deficit with debt mechanism (BRL 94.5 billion)..

Table 2 – ***Budget resources allocated for federal debt***

Budgetary Source	Primary Balance Identificator	Allocation	Description	BRL bn
100	Primary	Free-allocation	Ordinary Resources	86.2
188	Financial	Free-allocation	National Treasury’s Single Account earnings	67.8
159	Financial	Debt-exclusive	Official Credit Operations granted by the Treasury - Medium and Long-term Debt Service	40.8
173	Financial	Debt-exclusive	Official Credit Operations - Credit Operations Service - Subnational Governments	21.6
929	Primary	Free-allocation	Concessions and Permits	10.5
197	Primary	Debt-exclusive	Dividends from State-Owned Companies	7.5
-	Financial and Primary	Debt-exclusive and Free-wallocaiton	Others	0.5
Total				**234.9**

Source: *2019 Annual Budget Law Draft and National Treasury*

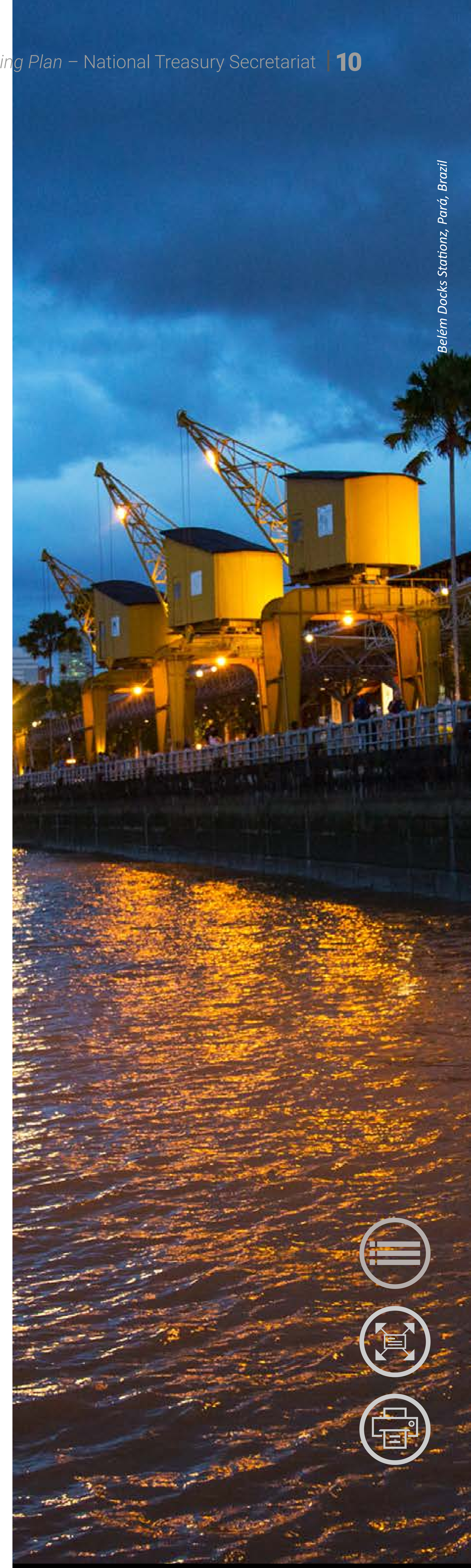
Potential resources arising from Central Bank's result (source 152) are not included in the computation of the borrowing requirements, due to their uncertain nature, associated with future exchange rate behavior, which results in a high degree of unpredictability.

The foreseen budgetary resources can be affected by underperformance in the source 173, that is of debt-exclusive use. This source concerns payments inflows originated by subnational governments debt services obligations. Underperformance can occur in case of contractual renegotiations, adherence to the Fiscal Recovery Regime or by the effect of preliminary injunctions. More information regarding this risk is available at the Annual Debt Report 2018, in the following link: https://www.gov.br/tesouronacional/en/federal-public-debt/domestic-market/auctions.

The borrowing requirements forecast does not include potential obligations related to contingent liabilities managed by the National Treasury under recognition process, since the time to complete the settlement is unforeseeable. The 2019 Budget Guidelines Law, in its Fiscal Risks Annex, indicates an expectation of BRL 13.3 billion, of which 93.98% are potential remaining liabilities of a ceased housing policy financial instrument.

> *The "liquidity cushion" is a management tool that serves to mitigate rollover risk in stress scenarios.*

Additionally to the resources forecast that will be allocated to the federal debt in 2019, the National Treasury holds a liquidity reserve, known as "liquidity cushion". These concerns resources ready for debt payment, available in BRL deposited into the Single Account. The cushion allows the National Treasury to manage against large maturities periods, reduce debt rollover risk and honor possible contingent liabilities. Currently, these resources would be enough to pay off debt maturities at least for the next six months. This reserve ensures management flexibility to act in the event of adverse conditions and excessive volatility in the government bonds market.



Belém Docks Stationz, Pará, Brazil

Praia do Canto de Cima, Vitória, Espírito Santo, Brazil

3 Federal Debt Strategy

3.1. Domestic debt

The 2019 *Annual Borrowing Plan* seeks to attain the debt management objectives and observe a set of qualitative guidelines that includes smoothing maturity profile, especially in the short-term, raising liquidity in the secondary market, enlarging investors' base, and increasing average maturity.

To improve federal debt profile, the strategy includes the issuance of fixed-rate bonds (LTN and NTN-F) and inflation-linked ones (NTN-B). The issuance of the latter supports debt lengthening guideline since these bonds have longer maturities.

To smooth maturity profile and to increase the liquidity in the secondary market of government bonds.

To promote the consolidation of liquid benchmarks, the 10-year NTN-B issuances throughout the year will remain maturing in August 2028, throughout the year. In the same line, the LTN maturing in July 2022 will continue to be issued during the first quarter of the year, serving as the 48-month benchmark. Subsequently, this benchmark will be represented by the introduction of LTN maturing in July 2023.

The federal debt planning also includes offering three different LFT benchmarks throughout the year, one at a time, aiming at the smoothing of maturities' concentration. LFT bonds play an important role in the federal debt rollover. They also contribute to the maintenance of Treasury's liquidity reserve at prudential levels, reducing rollover risk.

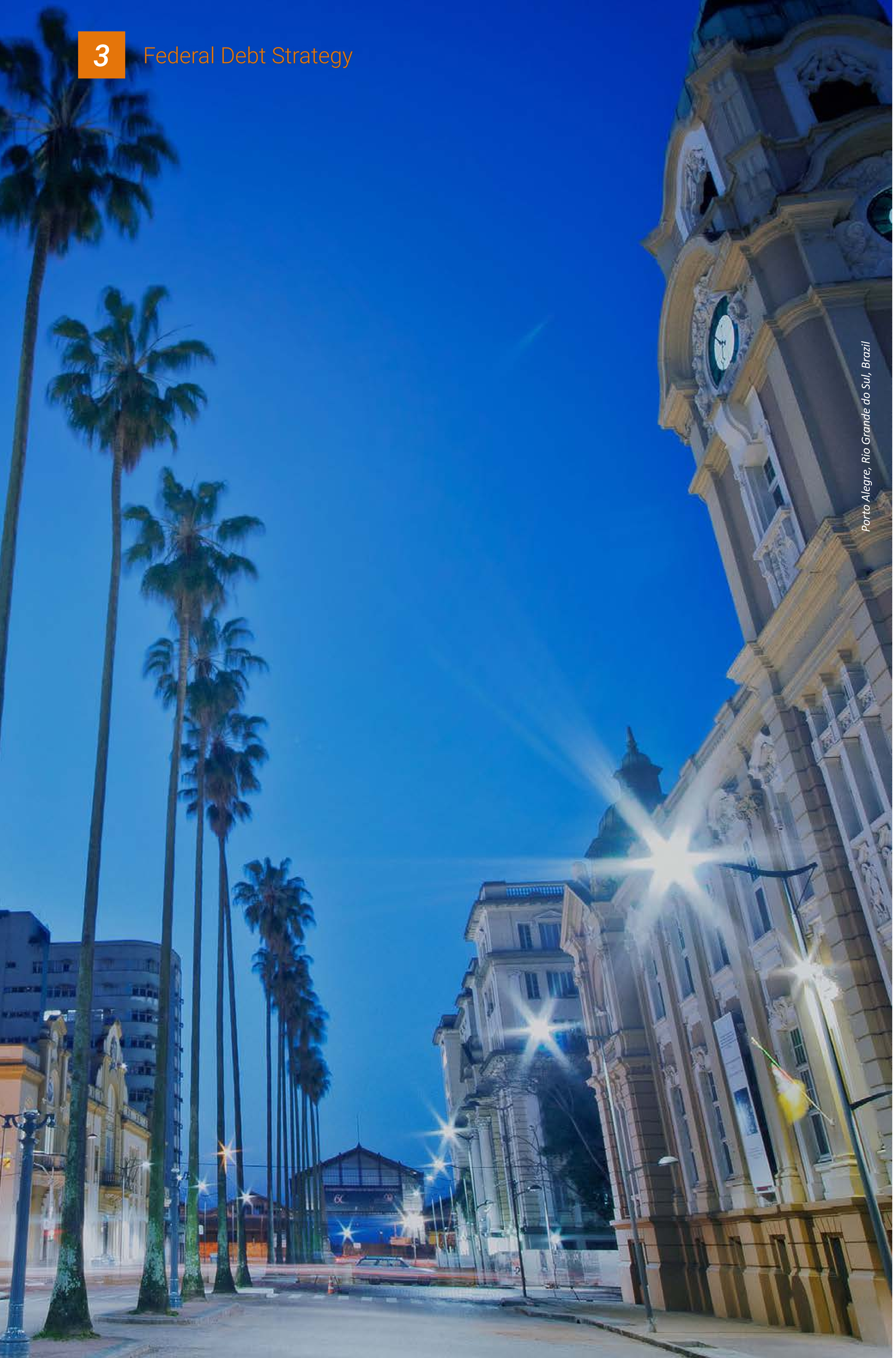
Considering the outstanding domestic federal bonds, the expectation to the year is to achieve a rollover percentage, covering both principal and interest charges, around 100%, so that debt management will not increase financial system liquidity. Table 3 presents the bonds' offers during 2019 for each reference period.

Table 3 – ***Benchmarks issuances in 2019****

Bond	Indexing	Interest Coupon	Benchmark and Maturities	
LTN	Fixed-rate	Zero coupon (interest is paid at maturity, corresponding to the difference between the issue value and the redemption value)	Short and Medium terms	6 months - Oct/2019 and Apr/2020
				12 months - Apr/2020 and Oct/2020
				24 months - Apr/2021 and Oct/2021
				48 months - Jul/2022 and Jul/2023
NTN-F	Fixed-rate	10% per year, payable semiannualy	Long term	7 years - Jan/2025
				10 years - Jan/2029
LFT	Floating-rate	Zero coupon (interest is paid at maturity according to index fluctuation)	Medium term	6 years - Mar/25, Sep/25 and Mar/26
NTN-B	CPI	6% per year, payable semiannualy	Group I – Medium term	5 years - Aug/2024
				10 years - Aug/2028
			Group II – Long term	20 years - May/2035
				40 years - May/2055

**For more details on the characteristics of domestic federal bonds, see Decree nº 9,292, of 2018.*
Source: *National Treasury*

Botanic Garden, Curitiba, Paraná, Brazil



Porto Alegre, Rio Grande do Sul, Brazil

The frequency and format of the auctions remain unchanged regarding to the previous year, as shown in Table 4.

Table 4 – ***Frequency of domestic federal bonds auctions to be carried out by the National Treasury in 2019***

Bond	Traditional		Exchange	
	Frequency	Selection Criterion*	Frequency	Selection Criterion
LTN	Weekly	Multiple Price		
NTN-F	Weekly	Multiple Price		
LFT	Fortnightly	Multiple Price		
NTN-B	Fortnightly	Uniform Price	Quarterly	Multiple Price

** Selection criterion for bids in the auctions: in the uniform criterion, all proposals with quotes equal or greater than the minimum accepted quote will be accepted, and the latter will then be applied to all winning bids. In the multiple price criterion, accepted bids pay the price submitted in the bid.*

Source: *National Treasury*

Considering the transparency and predictability of its activities, National Treasury publishes the Annual Auctions Schedule on its website. Notwithstanding, in executing its borrowing strategy, the debt manager continuously observes the prevailing conditions in the economy and in the financial markets and, at specific times, the planning can be adjusted. Eventually, National Treasury may choose to carry out unanticipated auctions to contribute to the proper functioning of the markets.

2019 Auctions Schedule

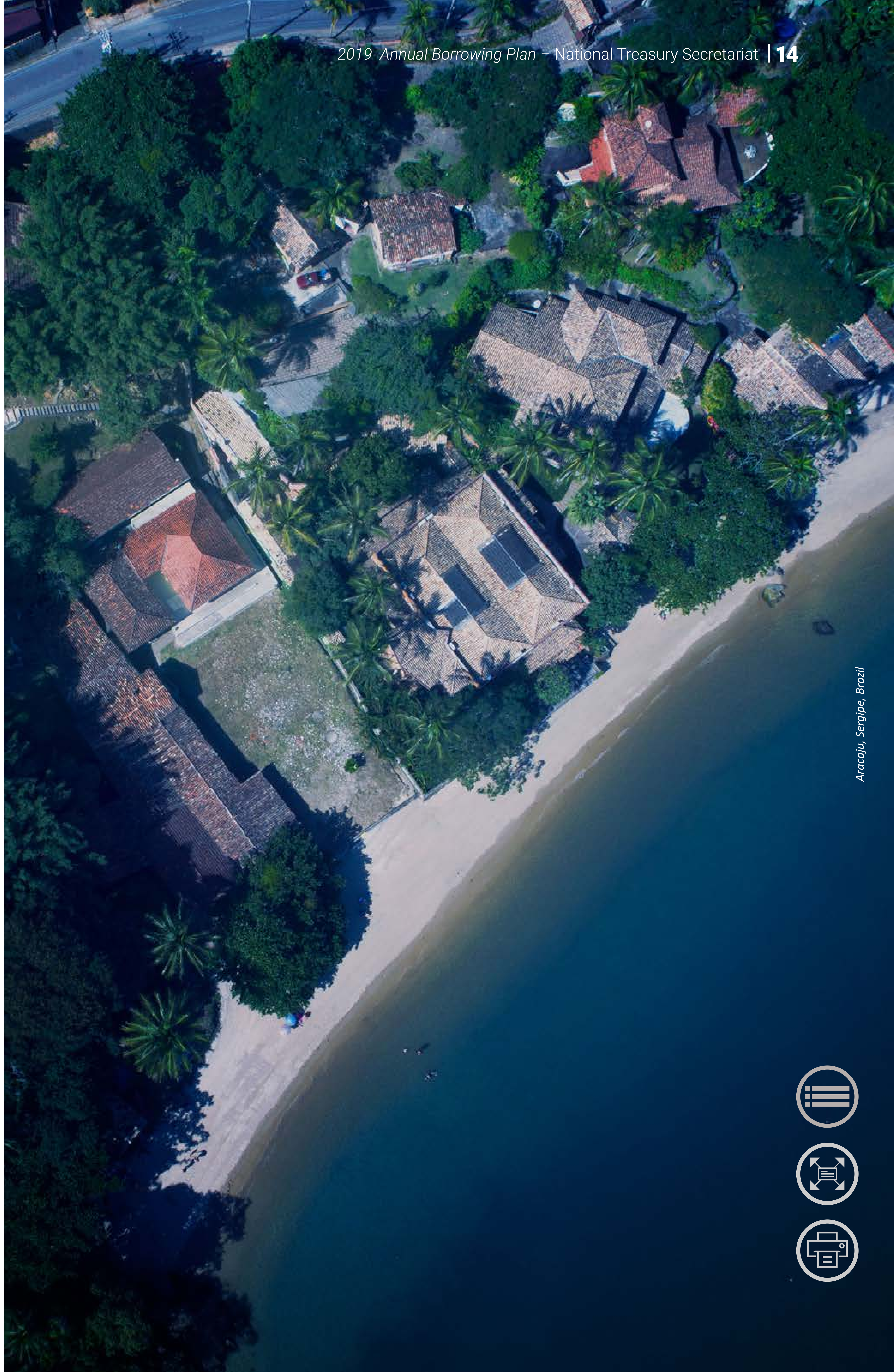
3.2. External debt

In 2019, National Treasury's operations in the international markets will continue to follow a qualitative guideline of consolidating liquid and efficient external yield curves, whose parameters can serve as reference for the corporate sector. Currently, Brazilian sovereign debt has benchmarks in dollar, euro and BRL.

For the improvement of the external yield curve, the National Treasury maintains the buyback program and may act through other liability management operations to withdraw less efficient bonds from the market. Thus, the Treasury contributes to the development of the term structure of interest rates not only in the domestic market, but also in the external one, in line with the federal debt guidelines.

Another point to highlight is that the rollover risk of the external federal debt in the short term has been mitigated, considering that all interest and principal disbursements for 2019 have already been previously financed, either with reserves from international issuances or through currency purchases in the local market.

Objectives and Guidelines for external debt



Aracaju, Sergipe, Brazil

4 Expected Results

Considering the strategies previously described, as well as the borrowing requirements and the prospected economic scenarios, Table 5 summarizes the expected results for the federal debt performance in 2019. The results are presented in the form of reference intervals to underline the importance of considering a certain degree of freedom in the public debt management. This allows the National Treasury to adjust its operations to the conditions prevailing in the bond market at any given time.

*Table 5 – **Reference intervals for federal debt in 2019***

Statistics	2018	Reference Intervals 2019	
		Minimum	Maximum
Outstanding Debt (BRL billion)			
FPD	3,877.1	4,100.0	4,300.0
Profile (%)			
Fixed-rate	33.0	29.0	33.0
Inflation-linked	27.5	24.0	28.0
Floating-rate	35.5	38.0	42.0
FX	4.0	3.0	7.0
Maturities Structure			
% Maturing in 12 months	16.3	17.0	20.0
Average Maturity (years)	4.1	3.9	4.1

***Source**: National Treasury*

4.1. Federal debt outstanding

The projected range for the outstanding debt at the end of 2019 reflects both the expectation of interest accrual and the planned results for issuances and redemptions throughout the year. Regarding domestic debt in the market, the strategy seeks to roll over around 100% of the principal and interest maturing in the period. This allows to prevent adding liquidity to the financial system.

4.2. Federal debt profile

The reference intervals for the federal debt profile in 2019 point to a cyclical situation. A deviation from the desired long-term composition is expected (see section 5.1 below). As a policy to reduce exposure to market risk, the federal debt guidelines require a diversified composition with a higher proportion of longer-term inflation-linked and fixed-rate bonds. In the short term, however, issuing more floating-rate bonds may be necessary to reach the approximate mark of 100% rollover of the maturing principal and interest for the year.

Ministries Esplanade, Brasília, Brazil

Market risk refers to the possibility of a rise in the outstanding debt due to fluctuations in interest rate, exchange rate and inflation that affect the costs of government bonds.

The 2019 *Annual Borrowing Plan* brings the possibility of placing higher volumes of fixed-rate and inflation-linked bonds, the latter at a lesser extent compared to the previous year. However, the composition intervals show the continuity in the trend, initiated in 2015, of an increase in the proportion of LFT in the outstanding federal debt, diluting the weight of the other debt instruments. The increase in the share of LFT is directly related to the recurrent primary fiscal deficits. Despite of representing greater exposure of public debt to variations on the reference interest rate (Selic), the LFT are issued with maturities of around six years and thus avoid the concentration of maturities in the short term, serving as an alternative to short-term fixed-rate bonds. The expected increase for 2019 in the relative share of LFT is more related to the low volume of maturing bonds, in the order of BRL 67.0 billion, than to an expectation of larger volumes of issuances compared to the previous year.

4.3. Federal debt maturity structure

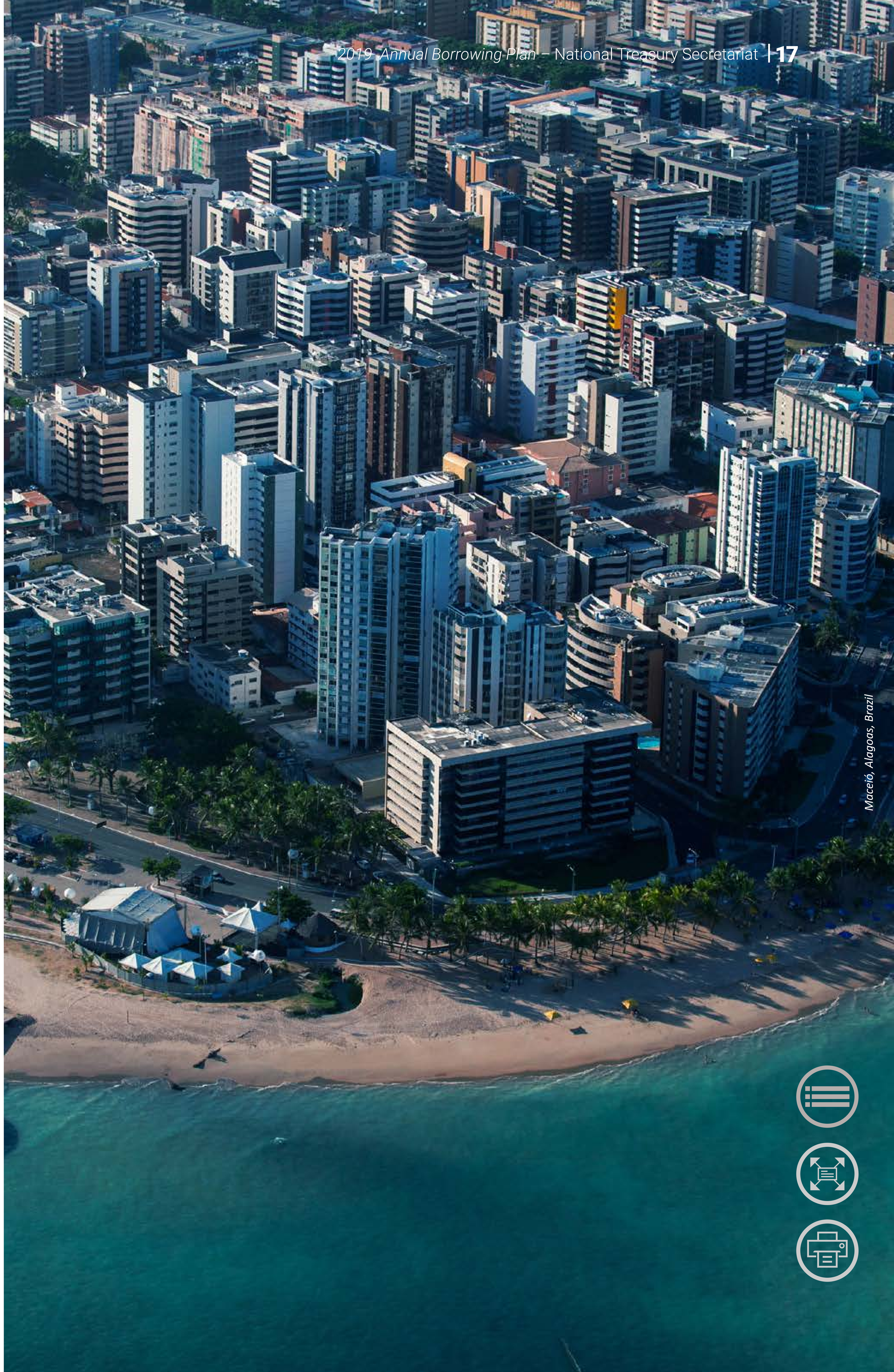
Federal debt maturity structure can be assessed by statistical indicators. Due to their simplicity and ease of communication, the percentage of outstanding debt maturing in one year and the outstanding average maturity also contribute to enhance the transparency of the risk management policy. While the former is a gauge for the debt maturing on the short term, the latter reflects the average remaining time for debt payments weighted by the present values of the principal and interest flows. The greater the amount of debt maturing in one year and the shorter average maturity, the higher the rollover risk.

Despite showing a slightly increase, the short-term debt indicator is expected to remain below 20%, which is a historically low level. Moreover, such a risk is mitigated by the maintenance of the liquidity reserve (“liquidity cushion”), which currently attains the equivalent of more than six months of the maturing outstanding domestic debt.

Debt rollover risk refers to the possibility of adverse conditions for the Treasury to roll over the maturing debt, or, in the limit, the impossibility of raising funds to honor its commitments.

In turn, the range for the outstanding federal debt average maturity has an expected average point of 4.0 years, suggesting a marginal reduction in relation to the 4.1 years registered at the end of 2018. The potential reduction of this indicator is associated with changes in the federal debt composition, particularly with the declining trend in the participation of inflation-linked bonds, that are typically longer average maturity instruments.

In addition to the average maturity statistic, the National Treasury regularly discloses the federal debt's average time to maturity. This indicator is useful for international comparisons, since many countries use this metric to calculate the maturity of their debts rather than the average maturity concept[2]. Information regarding alternative indicators to the federal debt is available at: https://www.gov.br/tesouronacional/en/federal-public-debt/about-federal-public-debt/key-figures-of-the-federal-public-debt



Maceió, Alagoas, Brazil

[2] *The average time to maturity (ATM) is a less efficient indicator than the average maturity one. The former neither considers intermediate interest coupons nor adjusts the principal flows to present values. These inaccuracies – which are the reason why lesser emphasis is given to this indicator in the federal debt statistics – imply that the ATM generates values higher than the average maturity. Despite these limitations, most countries adopt indicators similar to the ATM in their maturity profile statistics. Then, direct comparisons with the metrics used to set the reference intervals in this borrowing plan are not correct.*

5 Medium- and Long-term Perspectives for the Federal Debt

5.1. Federal debt in the long term

The definition of the long-term optimal profile for the federal debt (or benchmark portfolio) is the result of a quantitative exercise that points to a desirable position according to a chosen methodology. Its function is not to establish a composition that should be pursued immediately and at any cost, but rather to contemplate quantitative guidelines for the federal debt indicators. The benchmark portfolio is one of the main pieces of debt planning, complementing its objectives and its qualitative guidelines.

The benchmark portfolio is a guide for the design of financing strategies that considers the risk management and indicates the long-term desired reference values for the federal debt composition and maturity structure. As shown in the Table 6, those values remain the same as the previous year.

*Table 6 –**Indicative intervals for long-term optimal profile***

Statistics	Long Term Limits	
	Reference	Range
Profile (%)		
Fixed-rate	40.0	+/- 2.0
Inflation-linked	35.0	+/- 2.0
Floating-rate	20.0	+/- 2.0
FX	5.0	+/- 2.0
Estrutura de vencimentos		
% Maturing in 12 months	20.0	+/- 2.0
Average Maturity (years)	5.5	+/- 0.5

Source: *National Treasury*

5.2. Directions for the federal debt in the medium-term

Federal debt borrowing strategy in the coming years should consider the challenge of dealing with the increasing in public indebtedness. The Public Debt Forecast Report, to be published in Portuguese by the National Treasury three times a year, presents a medium-term scenario for the general government gross debt-to-GDP ratio, which contributes to enhance the transparency of public debt management and to guide market expectations regarding this indicator. The federal debt in the market, object of this borrowing plan, currently accounts for about 70% of the general government gross debt. This section explores the projections for federal debt indicators of composition and maturity structure for the next 10 years.

Medium-term projections reflect conjunctural challenges. From 2022 on, it is expected a movement towards the long-term optimal profile.

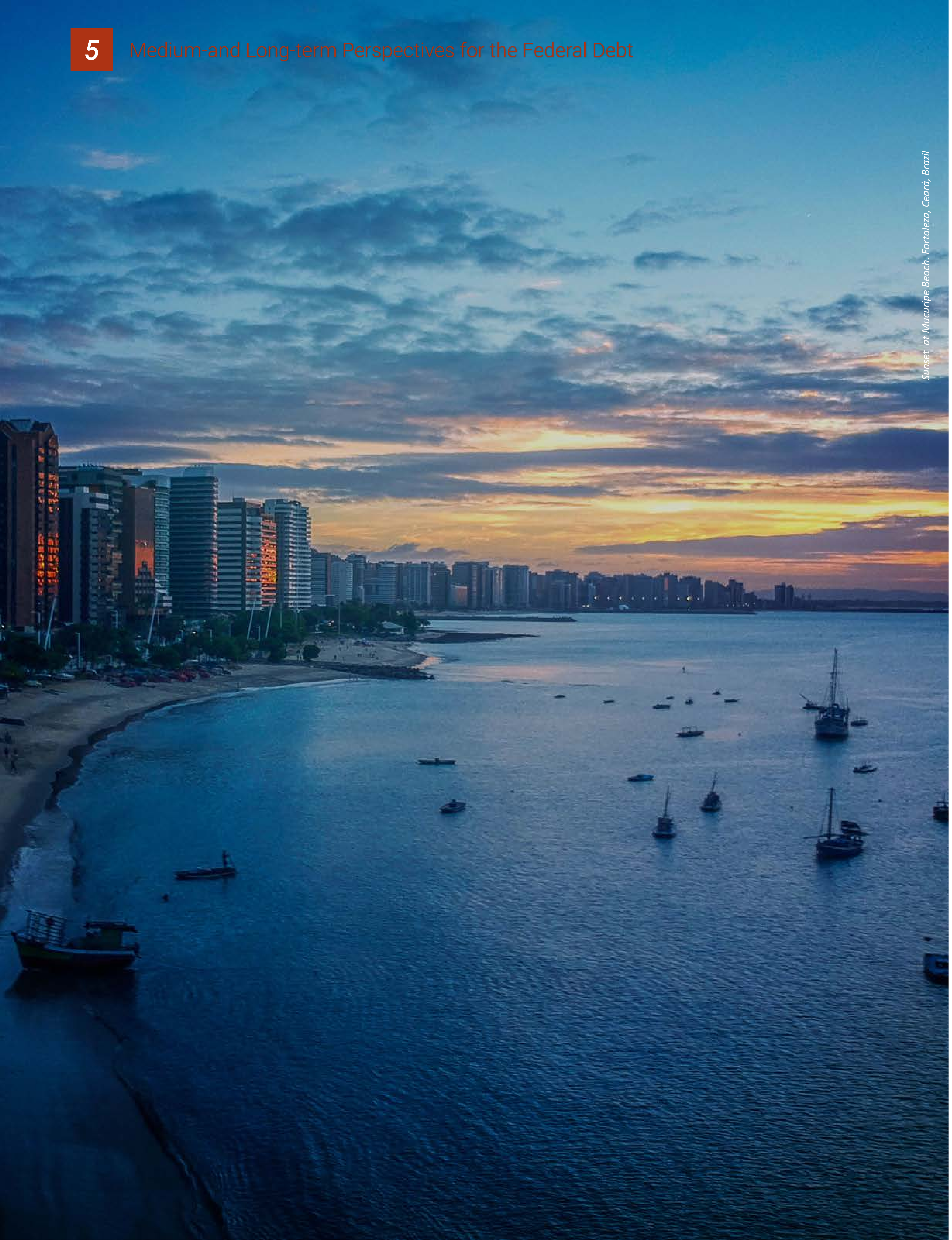
The path between the current situation and the long-term optimal profile is the scope of the federal debt medium-term planning. The exercise connecting the two horizons is based on the present information and on the forecast of economic variables, especially those concerning fiscal developments. However, this should not be interpreted as a goal-setting for future indicators.

Regarding the economic environment, the international outlook presents challenges and relevant volatility. The domestic scenario shows the recovery of economic activity and of agents' confidence, in a context of structural reforms promotion. An improvement in the fiscal side is part of such developments. However, the coming years will continue to require federal debt management to cover not only debt redemptions, but also borrowing requirements due to primary deficits.

Taking this scenario as a reference, the simulation of the medium-term strategy assumes the rollover of principal and interest around 100% over the whole planning horizon. Such an effort, even in scenarios of comfortable cash position, would prevent these maturities from injecting liquidity in the financial system. More than that, this policy, in combination with positive fiscal results, should contribute to the reduction of excess liquidity that is currently sterilized by the Central Bank through repurchasing operations (known as repos). This movement would represent an improvement in the general government gross debt composition, with a lower share of repos relative to the federal debt.

Indeed, this borrowing strategy also contributes to maintain the liquidity reserve at prudent levels, giving to the National Treasury flexibility to act in eventual moments of market stress. The policy of maintaining a comfortable cash position is essential for mitigating federal debt rollover risk.

The medium-term projections, shown in Figure 3, point to a time horizon initially marked by a debt profile that deviates



Sunset at Mucuripe Beach, Fortaleza, Ceará, Brazil

from the guidelines of the benchmark portfolio. The main reason is the rise in the share of floating-rate bonds in the federal debt. At a later stage, between the third and the fifth year, one observes a convergence back to the long-term optimal profile.

For this planning horizon, the National Treasury considers possible challenges, especially those emerging from more conservative scenarios, to the placement of longer-term fixed-rate and inflation-linked bonds in volumes that would speed the convergence towards the benchmark portfolio. The decision to fully rollover principal and interest payments implicates accepting higher share of floating-rate bonds in the first years of the planning horizon.

In the baseline scenario, from 2022 on, there would be room for a reversion to a debt trajectory more consistent with the desired long-term composition. As a counterpart to the increase in the share of floating-rate bonds in the coming years, the forecasts point to a decline in the share of fixed-rate bonds until 2020 and of inflation-linked bonds until 2021. At last, the share of foreign exchange debt in the federal debt is expected to stay at current levels.

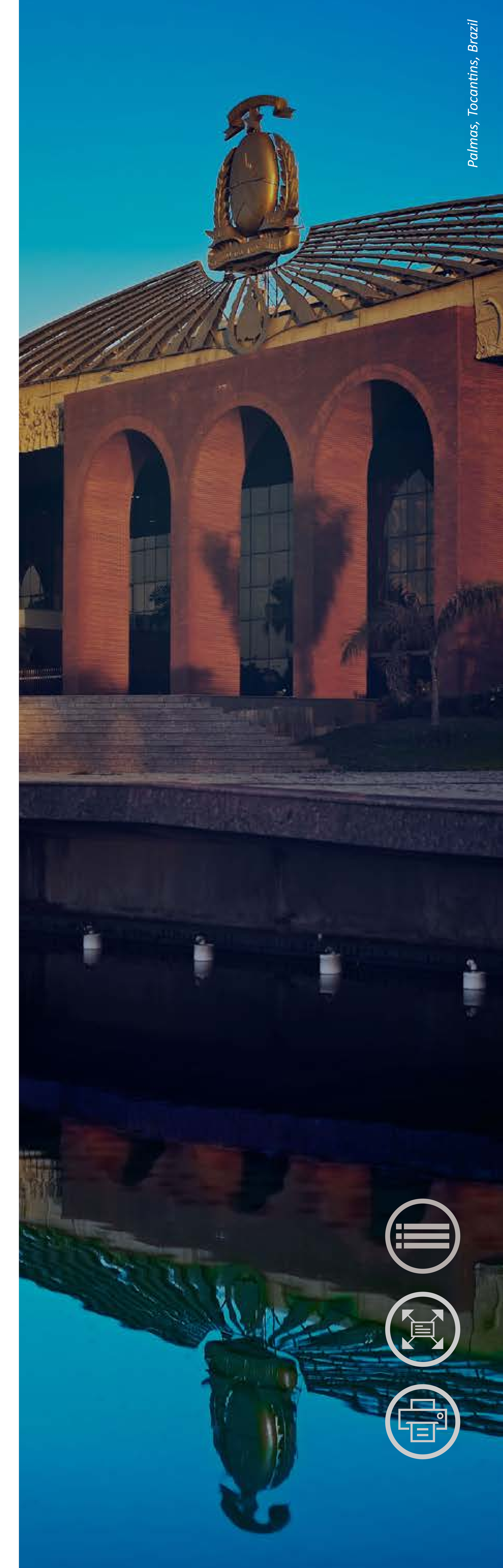
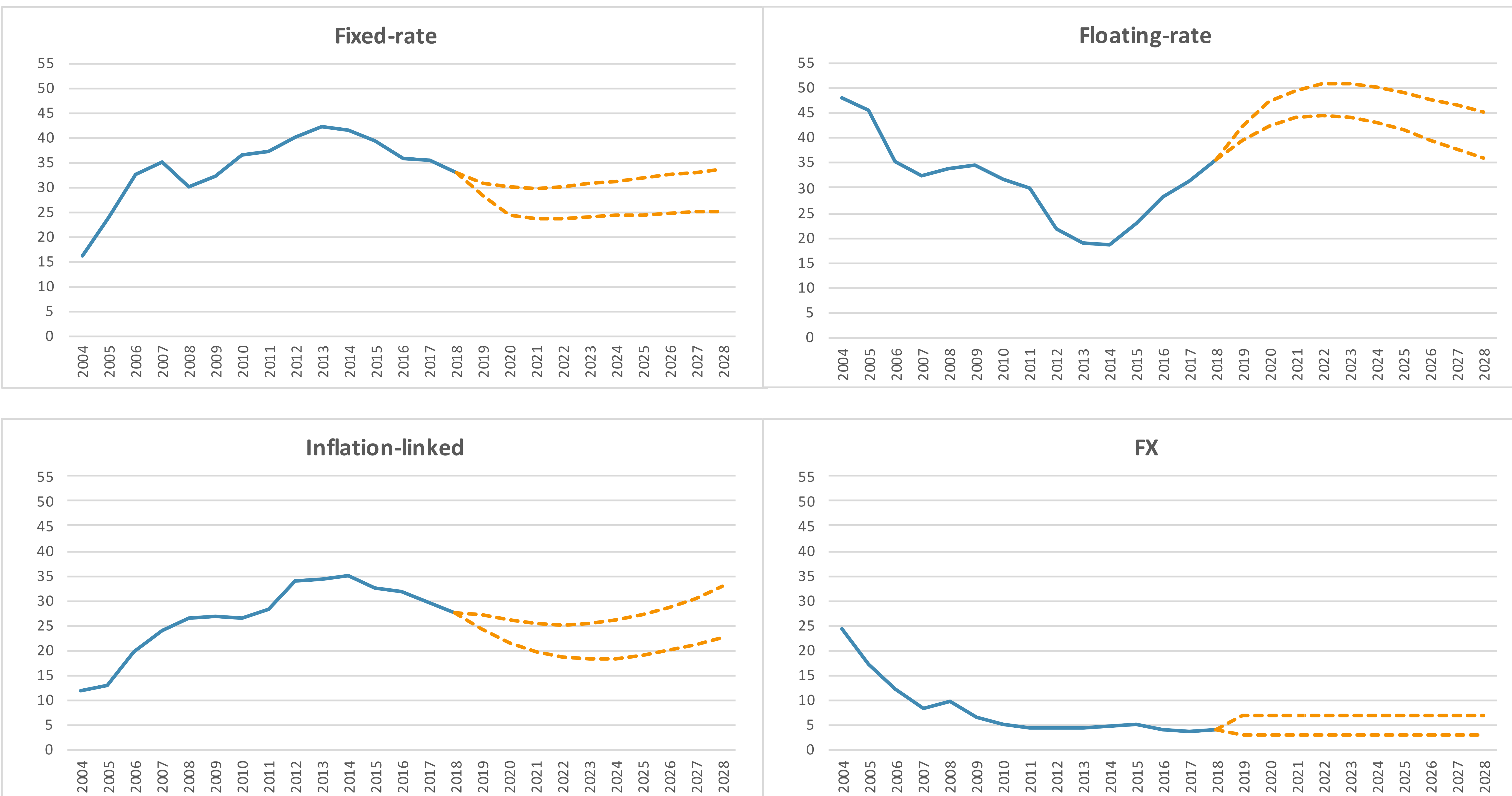


*Figure 3 – **Federal debt profile in the medium term (upper and lower limits - % FPD)***

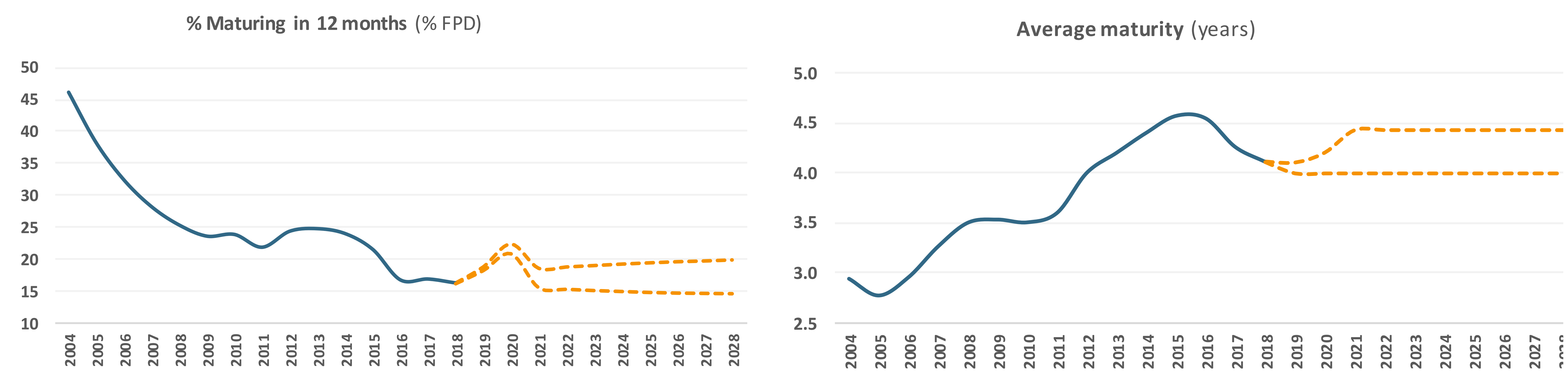


***Source:** National Treasury*

The maturity structure for the next 10 years should behave close to the long-term optimal profile, except for an oscillation in 2020, when an above-the-average volume of LFT matures and affects the share of debt maturing in one year. Nonetheless, the strategy is not impaired by such a deviation, especially when considering the support of the "liquidity cushion".

The average maturity, on the other hand, should be slightly reduced due to both possible demand restrictions for longer-term bonds in the first half of the planning horizon and investors' base profile changes. However, it does not fall below 4 years throughout the period. An improvement on this indicator in the direction suggested by the benchmark portfolio requires greater issuance of longer-term inflation-linked or fixed-rate bonds, which will be possible as economic conditions improve and the fiscal consolidation takes place. For an analysis of annual data on federal debt indicators, please refer to the Annual Debt Report.

Figure 4 – ***Federal debt maturity structure indicators on the medium term (upper and lower limits)***



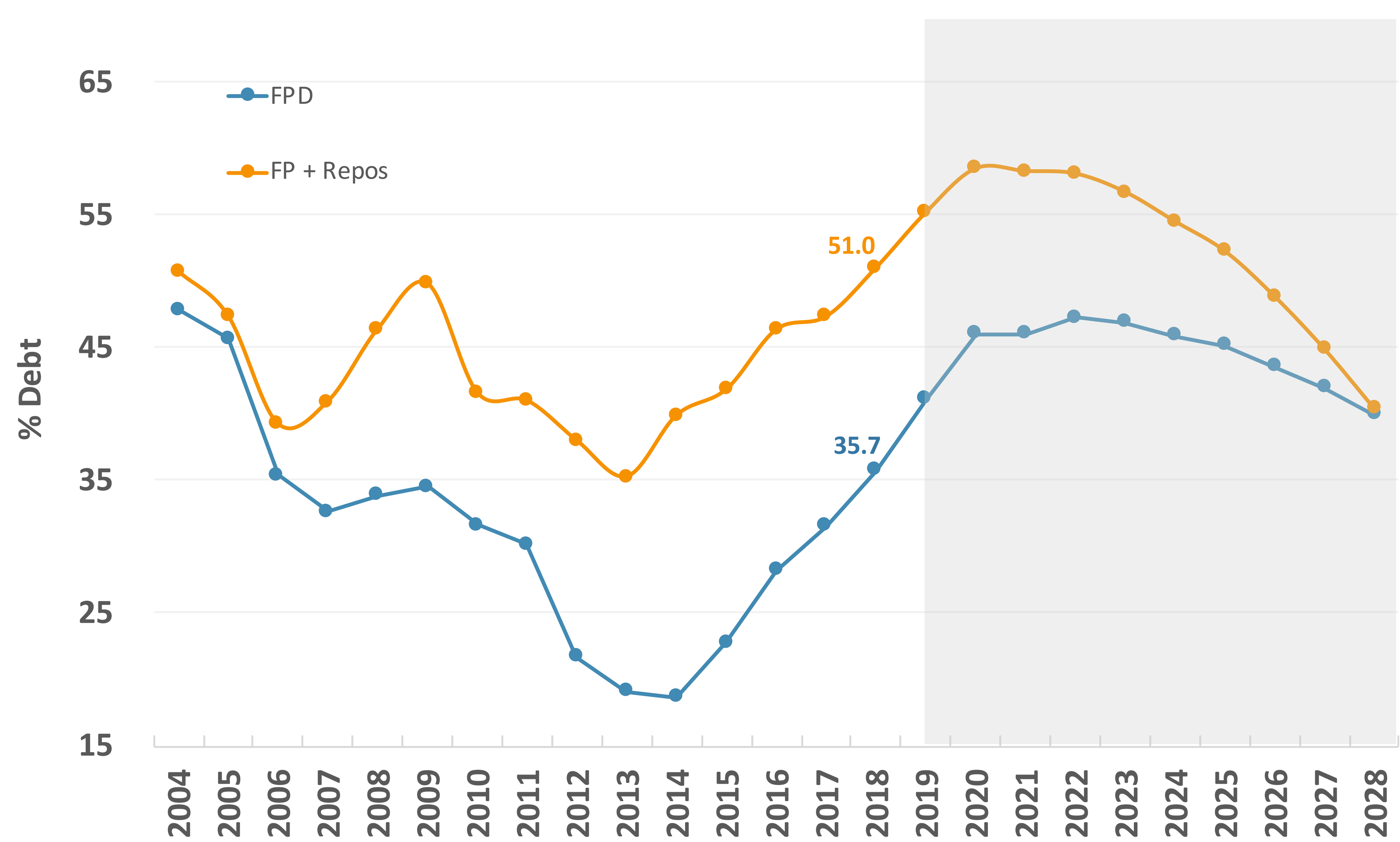
Source: *National Treasury*

5.3. A broader analysis of debt composition

The assessment of the share of floating-rate bonds, notably LFT, on public debt is an indicator of the interest rate risk for the National Treasury. Changes on the average cost of debt due to fluctuations in the reference interest rates will be proportional to the weight of those bonds in the federal debt. This view of risk, however, can be expanded to include other debt instruments that also have their cost sensitive to short-term interest rates. In this sense, the outstanding debt coverage can be expanded in the analysis to incorporate the repos, which are floating-rate instruments and are included in the general government gross debt statistics.

Figure 5 shows both the evolution of floating-rate bonds in the federal debt and the same measure when widening the concept of debt with the repos. For the coming years the LFT issuances will exceed redemptions, specially until 2020, so that the share of floating-rate bonds should rise until 2022. However, *ceteris paribus*, the broader debt concept, that includes repos, should not change significantly when the National Treasury issues more LFT to avoid increment financial system liquidity. Thus, in the evaluated scenarios, the outstanding debt including repos tends to stabilize as of 2020, falling more sharply after 2022, in a movement that follows the expected fiscal consolidation.

Figure 5 – ***Share of floating-rate liabilities in the federal public debt***



** Forecasted values correspond to the expected average points.*

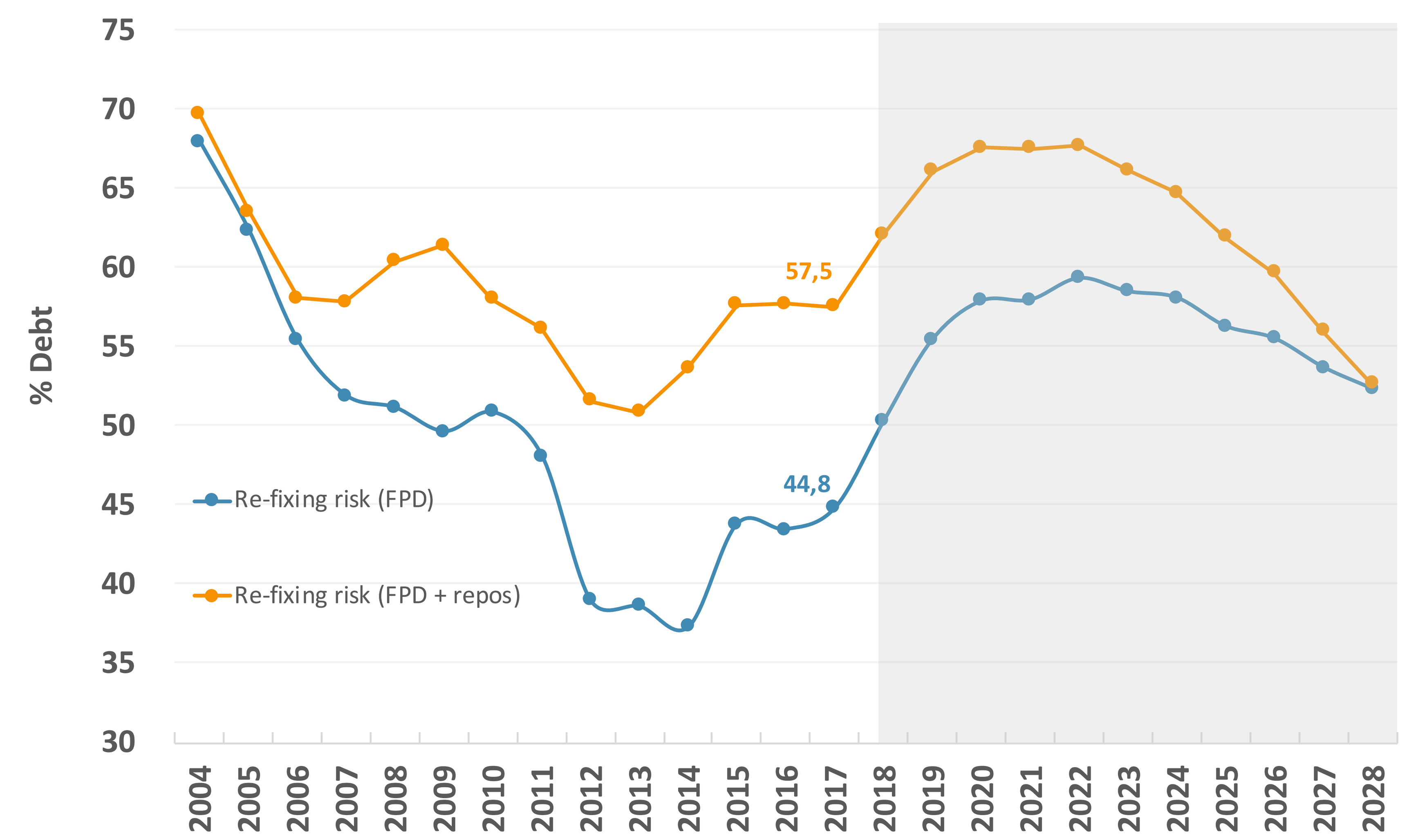
Source: *Central Bank and National Treasury*

An even more conservative perspective includes the interest rate re-fixing risk, which adds to the share of floating-rate bonds the share of federal debt maturing in one year. The re-fixing risk represents the portion of the outstanding debt that will have its cost redefined in the short term. Thus, it is an indicator that combines the effects of changes in both the debt profile and the maturity structure. The re-fixing risk would not be affected by the replacement of LFT with short-term fixed-rate bonds.

The tradeoff between LFT and short-term bonds becomes evident as the borrowing requirements met by other bonds instruments start to reach a demand constraint. From this point, the debt management must be attentive in not distorting the prices of government bonds. Given the relative prices, LFT would tend to have more weight in the debt management strategy compared to the short-term bonds, because it would have similar implications in terms of interest rate risk, but with LFT implying a lower cost for the Treasury.

The interest rate re-fixing risk showed a declining trend until 2013, whether considering the federal debt alone or including the repos. From there the indicator rises following the growth of debt outstanding itself. Initially, this movement is driven by repos. But from 2015 on the National Treasury performed issuances in volumes larger than maturities, mainly through the increase in the share of LFT. It is likely that this metric will start to fall again from 2022 on, combining a reduction of repos and LFT. A key premise for this development is the achievement of fiscal primary surpluses.

*Figure 6 – **Interest rate re-fixing risk***



** Re-fixing risk (FPD) = (FPD maturing in 12 months + LFT maturing from 12 months on)/FPD*
Re-fixing risk (FPD + Repos) = (Repos+ FPD maturing in 12 months + LFT maturing from 12 months on)/(FPD + Repos)

*** Forecasted values correspond to the expected average points.*

***Source:** Central Bank and National Treasury*

Amazonas Theater, Manaus, Brazil

6 Final remarks

The *2019 Annual Borrowing Plan* is published in a political and economic environment surrounded by expectations involving long-waited structural reforms. These reforms will enable Brazil to resume a path of sustainable economic growth, anchored in a fiscal policy capable of preserving the credibility of the State regarding its commitments. The short- and medium--term challenges remain relevant and the success in overcoming them depends on the efforts of the many stakeholders to implement fiscal adjustment.

By publishing the *Annual Borrowing Plan*, the National Treasury reaffirms not only its commitment to communicate with society but also to promote fiscal consolidation and uphold fiscal responsibility as a fundamental value.

Finally, in a constant effort to improve the transparency of the public debt management, the National Treasury welcomes and encourages suggestions to this report.

E-mail for suggestions:
ascom@tesouro.gov.br