

# Bloomberg

*“The government’s desire is to try to keep some investors out so as not to appreciate the real. Making more of [real-linked global bonds] available to investors helps them. It’s relatively cheap funding.”—A. Urbina*

- Yields on Brazil’s real-linked global bonds have fallen below that of their prior issuance last October
- Demand for these bonds has grown in response to the government’s recent increase in the IOF tax on local investments to 6%
- Silva Capital expects that the Brazilian government may come to market with a new issue of the globals to take advantage of the relatively cheap funding which they now provide

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When interviewed this week by Bloomberg News, Alejandro Urbina, Silva Capital’s lead fixed income portfolio manager, remarked that it would be in the interests of the Brazilian Government to come to market with a new issue of its real-linked global bonds. Demand for these instruments, which allow investors to gain real exposure while conducting their transactions exclusively in dollars, has strengthened in recent months, lowering yields below the critical level of prior issuance last October.

While demand for real-exposure of all types has grown over the last year in line with the currency’s appreciation and the country’s growth, the particular gains of Brazil’s real-linked globals is more a product of its public policy than its macroeconomics. Hoping to shield exporters from the negative effects that a strong currency could have on their business, in 2009 the Brazilian Government levied an IOF tax on foreign investors looking to take advantage of the country’s local markets. By steering them clear of local BRL investments, the government hoped to ease FX pressure on the real and curb its appreciation. As the IOF tax has now risen to 6%, its disincentive has become sufficiently onerous that some investors seeking exposure to real have opted for alternative methods, such as the BRL-linked globals. Accordingly, yields on these bonds have declined.

It is possible that that the U.S. dollar will remain weak for some time, and as Brazilian economic fundamentals continue to be supportive of its currency, it is likely that the real will make further gains. We therefore expect that the Brazilian government will maintain its taxation of local capital inflows in order to slow further appreciation. In this case, the market for the real-linked globals will only deepen, and the government will have an increased incentive to fund itself with the comparatively low yields to be found there.

The reality is that Brazil has been seeking further issuance of BRL-linked external bonds for some time. It actively queried international investors about their interest at the time of the IMF meetings last year and re-tapped the 28’s soon after. We expect that the government may use the upcoming IMF gathering in Washington to gauge the actual interest for another re-tap or perhaps even the new issue of a longer-dated bond to expand the curve.