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# BRAZIL MACRO

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## SPECIAL REPORT

# FIRST MILE ON A LONG, WINDING ROAD

**Jankiel Santos**
jankiel.santos@santander.com.br
+5511 3012 5726


- The new regulatory framework for the FX market outlined by Law #14,286, which was sanctioned at the end of 2021, will become effective only at the end of this year in accordance with Article #29. The time lag will be used to implement various decrees, ordinances, etc., to allow the changes in the current legal structure, which bears some instructions instated more than a hundred years ago.
- The law will bring some (positive) changes aimed at making Brazil's FX operations less bureaucratic and much more aligned to the current business environment. We see improvements from the institutional, as well as companies' and citizens', standpoints to the functioning (and competitiveness) of the FX system.
- However, the new regulatory framework will not grant immediate authorization to everyone to open banking accounts in foreign currencies in the domestic financial system, allowing the currently sanctioned sectors to maintain such accounts for the time being. Therefore, the full convertibility of the BRL remains an objective for the long run, but the changes to be implemented should pave the way for such backdrops to materialize.
- In this piece, we present what we believe are the main changes pertaining to different segments, as well as some peculiarities or possible implications of these alterations.


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**Simpler, cheaper and more efficient**

After a little more than two years of appraisals, the draft-bill presented by the Brazilian Central Bank (BCB) in September 2019 proposing a revamp in the regulatory framework of the Brazilian FX market turned into law on December 29, 2021 and it was published in the official gazette the following day (Law #14,286). However, because of the depth of the changes the law will ensue, its last article stated that it will become effective only one year after its sanction (the so-called *vacatio legis* in the Brazilian legal system). It means that players of the Brazilian FX market will have about a year to get acquainted with all decrees, instructions and ordinances to be published and that will detail several issues the new law just outlined.

The rational for the draft-bill was to simplify the lives of all players, who have to deal with an outdated and complex structure bearing some directives introduced in 1920. In some cases, these directives are laid in laws that only touch on the topic of the FX, which turns any change into a knotty and protracted process—as it demands the entire piece of legislation to get through Congress. Law #14,286 will change a large number of existing laws and revoke 24 more in their entirety, granting to BCB the autonomy to regulate in general terms the FX market from 2023 onwards. By unifying and modernizing these rules and ascribing the decisions about

FX themes to the BCB's responsibility, one expects new improvements in the FX legislation to occur in a faster, safer and more technical fashion.

However, the new rules will not grant immediate permission to everyone to open a banking account in foreign currency in the domestic financial market. There will continue to be a limited scope of players allowed to open accounts in foreign currency (as stated by the BCB[1] itself), which means the full convertibility of the BRL shall remain a long-term objective for the country. Nonetheless, we think Law #14,286 should facilitate the transition for this new environment for the BRL in the future.

In order to assess the main changes and its impacts, we present them in distinct sections pertaining to each specific segment the change(s) refers to.

## INSTITUTIONAL ENVIRONMENT

As mentioned above, the key alteration brought by the new regulatory framework was to put under a unique "legal umbrella" all the directives that will guide the FX market in Brazil, as these rules are currently spread in many legal instruments. Consequently, it will become easier for the BCB, which will have full control of the directives, to implement changes in the FX directives if it feels necessary. In the following table, we display other changes that we judge are important in the institutional environment:

**Figure 1. Changes in the Brazilian institutional environment for the FX market brought by Law #14,286[2]**

| Initiative | Currently | From 2023 onwards | Observation / Implication |
|---|---|---|---|
| Definition of requirements for banking account in foreign currencies | National Monetary Council (CMN) and BCB | Exclusively BCB | It does not alter the current situation, but it makes it easier for changes to happen in the future. |
| Foreign capital registration | Required | Required | Although information is still required, the Law #14,286 opens room for BCB to simplify the process. |
| Compulsory FX contract | Required | Required | |
| FX deals codes | Required | Required | |
| Regulation of residents and non-residents' banking accounts | Differentiated | Equal | - - |
| Private clearing of claims or values | Prohibited | To be regulated | BCB will set specific conditions in which private clearing may happen. |

Source: BCB, Santander.

## FINANCIAL INSTITUTIONS

The new FX market regulatory framework should be of paramount importance for the growth of locally based financial institutions, as it will allow them to use funds raised in the domestic market to amplify their supply of services abroad, thus spreading the presence of BRL in international deals. Consequently, as these operations increase, the closer the full convertibility of the BRL will be. Applying the same logic, the authorization for international banks holding banking accounts in BRL to carry out money orders for the companies located abroad (full banking correspondence) is also a step towards increasing the international relevance of the BRL aimed at reaching its full convertibility. Last but not the least, Law #14,286 also brought innovations regarding the documentation and registration of FX operations, which should reduce the red tape currently related to them, thus making them simpler and cheaper.

[1] **Brazilian Central Bank's press release #2425** – December 31, 2021 – Available on: https://www.bcb.gov.br/en/pressdetail/2425/nota
[2] **Brazilian Central Bank** – December 31, 2021 – Available on: https://www.bcb.gov.br/content/about/legislation_norms_docs/Law_FX_14.286.pdf

**Figure 2. Main changes in the FX market for financial institutions brought by Law #14,286**

| Initiative | Currently | From 2023 onwards | Observation / Implication |
|---|---|---|---|
| Use of funds raised in the domestic market in international markets | Prohibited | Authorized | Locally based institutions will bear more firepower to provide services abroad. |
| Full bank correspondence | Authorized only for money orders directed to Brazil | Authorized for money orders in any direction | The BRL will start to circulate abroad, which is the first step towards its full convertibility. |
| Requirement of clients' documents already available | Authorized | Prohibited | - - |
| Classification of FX operations | Banks' responsibility | Clients' responsibility | - - |
| Support to clients for the classification of FX operations | Exempt | Required | - - |

Source: BCB, Santander.

## CORPORATE SECTOR

The goal of reducing bureaucracy and amplifying the integration of the Brazilian economy with the international economy is also present in the changes pertaining to the corporate sector. Nonetheless, most of changes are yet to be regulated by the BCB.

**Figure 3. Main changes in the FX market for the corporate sector brought by Law #14,286**

| Initiative | Currently | From 2023 onwards | Observation / Implication |
|---|---|---|---|
| Remittances of profits & dividends, interest payments and royalties payments | Registration + Tax payment | Tax payment | Still to be regulated by the BCB. |
| Payments in foreign currencies | Highly restricted | Highly restricted | CMN may enlarge the list of authorized operations. |
| Use of export revenue | Investments and payment obligations allowed | Loans will also be allowed | Still to be regulated by the BCB. |

Source: BCB, Santander.

## HOUSEHOLDS

The changes related to households were just a few and were also directed towards increasing the integration and the use of different currencies in the country, serving as a preparation for a full convertibility of the BRL in the future. As with the alterations pertaining to the corporate sector, there are themes which are still dependent on further regulation by the BCB.

**Figure 4. Main changes in the FX market for households brought by Law #14,286**

| Initiative | Currently | From 2023 onwards | Observation / Implication |
|---|---|---|---|
| FX transactions of small amount | Prohibited | ≤ US$ 500 | - - |
| Cash limit for tourists to leave/arrive the country | ≤ R$ 10K | ≤ US$ 10K or the equivalent amount in other foreign currencies | - - |

Source: BCB, Santander.

**CONCLUSION**

Although Law #14,286 will take a year to become effective and, initially, it did not mean a complete overhaul of the bureaucratic and knotty Brazilian FX rate market, the new regulatory framework that it ensues should pave the way for a much more efficient, cheaper and simpler system in the near future. Moreover, it should foster a stronger integration of the Brazilian economy with the international economy as well as lead to a higher usage of the BRL offshore. This combination should contribute towards the ultimate goal of having a fully accepted and convertible currency in the future. It will be a long-winded road until the country get there, but at least it has already crossed the first mile.

# CONTACTS / IMPORTANT DISCLOSURES


| Brazil Macro Research | | | |
|---|---|---|---|
| Ana Paula Vescovi* | Chief Economist | anavescovi@santander.com.br | 5511-3553-8567 |
| Mauricio Oreng* | Head of Macro Research | mauricio.oreng@santander.com.br | 5511-3553-5404 |
| Jankiel Santos* | Economist – External Sector | jankiel.santos@santander.com.br | 5511-3012-5726 |
| Ítalo Franca* | Economist – Fiscal Policy | italo.franca@santander.com.br | 5511-3553-5235 |
| Daniel Karp Vasquez* | Economist – Inflation | daniel.karp@santander.com.br | 5511-3553-9828 |
| Tomas Urani* | Economist – Global Economics | tomas.urani@santander.com.br | 5511-3553-9520 |
| Lucas Maynard* | Economist – Economic Activity | lucas.maynard.da.silva@santander.com.br | 5511-3553-7495 |
| Felipe Kotinda* | Economist – Commodities | felipe.kotinda@santander.com.br | 5511-3553-8071 |
| Gabriel Couto* | Economist – Special Projects | gabriel.couto@santander.com.br | 5511-3553-8487 |
| Fabiana Moreira* | Economist - Credit | fabiana.de.oliveira@santander.com.br | 5511-3553-1325 |
| Gilmar Lima* | Economist – Modeling | gilmar.lima@santander.com.br | 5511-3553-6327 |
| **Global Macro Research** | | | |
| Maciej Reluga* | Head Macro. Rates & FX Strategy – CEE | maciej.reluga@santander.pl | 48-22-534-1888 |
| Juan Cerruti * | Senior Economist – Argentina | jcerruti@santander.com.ar | 54 11 4341 1272 |
| Ana Paula Vescovi* | Economist – Brazil | anavescovi@santander.com.br | 5511-3553-8567 |
| Juan Pablo Cabrera* | Economist – Chile | jcabrera@santander.cl | 562-2320-3778 |
| Guillermo Aboumrad* | Economist – Mexico | gjaboumrad@santander.com.mx | 5255-5257-8170 |
| Piotr Bielski* | Economist – Poland | piotr.bielski@santander.pl | 48-22-534-1888 |
| Mike Moran | Head of Macro Research. US | mike.moran@santander.us | 212-350-3500 |
| **Fixed Income Research** | | | |
| Juan Arranz* | Chief Rates & FX Strategist – Argentina | jarranz@santanderrio.com.ar | 5411-4341-1065 |
| Mauricio Oreng* | Senior Economist/Strategist – Brazil | mauricio.oreng@santander.com.br | 5511-3553-5404 |
| Juan Pablo Cabrera* | Chief Rates & FX Strategist – Chile | jcabrera@santander.cl | 562-2320-3778 |
| **Equity Research** | | | |
| Miguel Machado* | Head Equity Research Americas | mmachado@santander.com.mx | 5255 5269 2228 |
| Alan Alanis* | Head. Mexico | aalanis@santander.com.mx | 5552-5269-2103 |
| Andres Soto* | Head. Andean | asoto@santander.us | 212-407-0976 |
| Claudia Benavente* | Head. Chile | claudia.benavente@santander.cl | 562-2336-3361 |
| Walter Chiarvesio* | Head. Argentina | wchiarvesio@santanderrio.com.ar | 5411-4341-1564 |
| Mariana Cahen Margulies * | Head. Brazil | mmargulies@santander.com.br | 5511 3553 1684 |
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