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BRAZIL MACRO

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GDP PREVIEW

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Modest 2Q21 GDP Growth Expected

- **Negative market surprises seen in the broad activity index (IBC-Br) in April and May (including sequential contraction) were in line with our scenario of modest 2Q21 GDP growth.** However, June's positive surprise in the IBC-Br release motivated us to raise our projection to +0.2% QoQ-sa from a flat 0% QoQ-sa.
- **On the supply side, we expect the services sector to post solid growth in 2Q21, stemming both from expansion in cyclical and non-cyclical segments, as the health crisis gradually subsides and mobility returns to "normal".** On the other hand, we anticipate that farm and industrial output will drag down activity in the short term, partially offsetting the tertiary sector's positive performance.
- **On the demand side, we expect household consumption to climb in 2Q21, on the heels of expansion in retail sales and services to families.** Moreover, we expect the external sector to contribute positively. Conversely, investments should retreat at the margin, reflecting a sequential fall in capital goods domestic production and imports.
- **If our projection is confirmed, this result would imply a carryover of 5.1% to 2021, placing the economy at levels 0.2% above the pre-crisis mark (4Q19).** Additionally, this result could give a little upside boost to our current 2021 GDP projection (5.1%), though we acknowledge the downside risks wrought by the drought for both electricity generation and agriculture output in 2H21.

Positive 1Q21 figure can be attributed to all the three main sectors that make up the GDP, yet less cyclical farm output provided the largest contribution (on the supply side). For 2Q21, however, we expect some heterogeneity in the composition of economic activity. Since the release of 1Q21 GDP results (June 1), our baseline scenario has forecast that the tertiary sector will contribute positively, on the heels of a faster-than-expected recovery of urban mobility and a new round of Emergency Aid. However, we expected farm output to partially give back its positive GDP contribution and industry to be a short-term drag on the recovery, reflecting cost increases and the widespread shortage of inputs. The negative market surprises seen in the IBC-Br (BCB's monthly GDP proxy) in April and May (including with a 0.6% monthly contraction) were in line with our expectations, but June's higher-than-expected climb implied slight quarterly growth (IBC-Br grew 0.1% QoQ-sa). While in qualitative terms, this was still in line with our expectation of modest 2Q21 GDP results, the upside surprise motivated us to raise our projection to +0.2% QoQ-sa from a flat 0% QoQ-sa.

On the supply side, we expect the services sector to post solid growth (1.0%) in 2Q21. As opposed to the previous quarter (when only cyclical services posted healthy figures), we expect more cyclical segments (such as Transports and Retail) to climb alongside non-cyclical segments (such as Health and Education services), as the health crisis gradually subsides and mobility returns to "normal". However, the tertiary's sector positive performance should be almost fully offset by weak figures for farm (-2.5%) and industrial output (-2.0%), dragging down short-term activity. The latter reflects the cost increases and widespread shortage of inputs in manufacturing, which should retreat 3.0% in 2Q21, but is partially mitigated by mining's favorable performance, which should grow 4.2%, on the heels of the positive commodity cycle.

On the demand side, we expect household consumption to be in the spotlight, climbing 1.2% QoQ-sa, reflecting solid expansion in broad retail sales (+3.0%) and services to families (+3.6%) in 2Q21, on the heels of economy's reopening and the payment of the new round of Emergency Aid. Government consumption should contribute positively, as the provision of public services (such as non-mercantile health and education services) gradually recovers. The external sector also should contribute positively, reflecting the solid increase of exports (6.3%) not fully offset by the climb in imports (5.8%). On the other hand, investments should retreat at the margin, reflecting the weak figures seen for domestic production and imports of capital goods. It's worth saying that, in stark contrast to the 1Q21 release, when the proxy of inventories replenishment (+2.0%) boosted GDP, our 2Q21 forecast is consistent with a negative contribution from inventories (-0.4%) on the final result.

If our projection is confirmed, this result places the economy at levels 0.2% above the pre-crisis mark (4Q19), and we calculate a 5.1% carryover left to 2021. After returning to pre-crisis levels in 1Q21 — boosted by less cyclical farm output — the GDP headline consolidates a full recovery, but still with some gaps in the composition (mainly in the services) to be filled ahead. Indeed, some segments of the services sector (Transports, Other Services and Public Services) are still running at depressed levels (down 0.8%, 8.7% and 4.1%, respectively), and their recovery could take place after vaccination advances, mobility returns to "normal" and the health crisis gradually ebbs. This gap to be filled along with the 5.1% calculated carryover left for 2021 imparts little upside risks to our current 2021 GDP projection (5.1%). However, we acknowledge the downside risks of the drought for both electricity generation and agriculture output in 2H21. **For details on Santander's activity outlook, please refer to our last chartbook[1].**

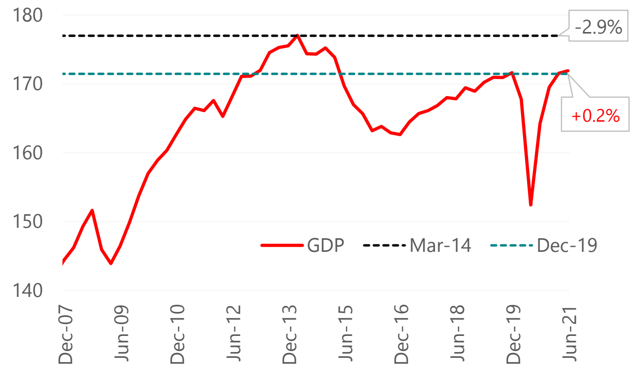
Figure 1. GDP Projections Breakdown

	1Q21		2Q21e		2021e	Pre-Crisis*
	% YoY	% QoQ	% YoY	% QoQ	% Carryover	% 4Q19
GDP	1.0	1.2	12.8	0.2	5.1	0.2
Supply						
Taxes	1.9	2.1	21.2	1.5	8.7	3.8
Agriculture	**5.2**	**5.7**	**1.9**	**-2.5**	**2.8**	**3.1**
Industry	**3.0**	**0.7**	**16.8**	**-2.0**	**4.1**	**-0.2**
Mining	-1.3	3.2	5.5	4.2	3.3	0.2
Manufacturing	5.6	-0.5	24.7	-3.0	4.1	1.2
Construction	-0.9	2.1	8.3	0.1	3.2	-2.8
Utilities	2.1	0.9	9.4	0.8	3.5	3.2
Services	**-0.8**	**0.4**	**11.4**	**1.0**	**3.7**	**-0.9**
Retail	3.5	1.2	23.0	1.6	8.3	5.0
Transports	1.3	3.6	25.4	0.3	9.5	-0.8
Information	5.5	1.4	12.5	3.2	7.6	7.0
Financial	5.1	1.7	1.1	0.2	3.0	5.4
Other Services	-7.3	0.1	14.0	0.9	3.4	-8.7
Rents	3.9	1.0	2.0	-0.6	2.0	4.0
Public Services	-4.4	-0.6	4.7	0.4	0.6	-4.1
Demand						
Consumption	**-1.7**	**-0.1**	**12.9**	**1.2**	**3.8**	**-2.0**
Government	**-4.9**	**-0.8**	**3.5**	**0.5**	**-0.2**	**-4.4**
Investments	**17.0**	**4.6**	**38.6**	**-1.0**	**19.6**	**18.1**
Exports	**0.8**	**3.7**	**11.1**	**6.3**	**7.1**	**5.5**
Imports	**7.7**	**11.6**	**30.9**	**5.8**	**23.7**	**14.4**

Sources: IBGE, Santander estimates.

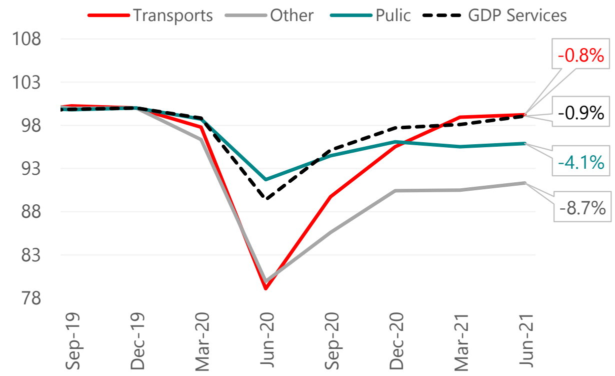
[1] **Santander Brazil Economic Activity - *"Chartbook – A Brighter Outlook for Mobility and Services"* –** August 18, 2021 - Available on: https://bit.ly/Std-chart-econact-aug21

Figure 4.A. – GDP (sa, average 1995=100)



Sources: IBGE, Santander Estimates.

Figure 4.B. – Services below the pre-crisis mark (sa, 4Q19=100)



Sources: IBGE, Santander Estimates.

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