DATA ANALYSIS – EXTERNAL SECTOR

WILL EXPORTERS EVER RETURN?

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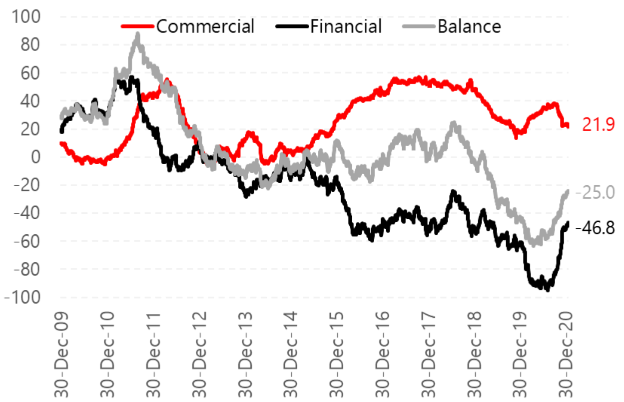
- **The spot FX market's registered net inflow of USD3.6 billion underpins our view that Brazilian external sector fundamentals are not compatible with the behavior of the BRL,** especially as its seasonally adjusted figures hint at a relatively balanced situation for the spot FX flow in the near term.
- **Despite this constructive backdrop, the gap between the "physical" trade balance and the net financial commercial flow continues to widen,** thus puzzling market participants and leading us to ask: **what will lure exporters to repatriate — at least some of — that money?**

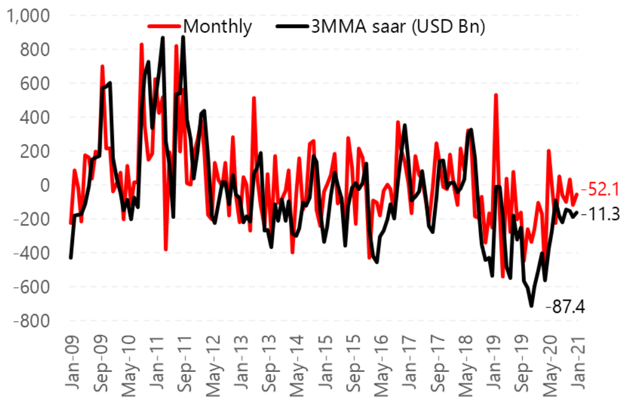
The Brazilian spot FX market recorded net inflow of USD3.6 billion in January 2021, as the commercial segment — which refers to trade-related flows — posted a net exit of USD0.8 billion in the period, whereas the financial segment recorded the arrival of USD3.6 billion. Adjusting data for the number of trading days, we find that the average net balance of the commercial segment (negative USD41 million) ran lower than the year-ago level (positive USD52 million), with financial average flows flowing in the opposite direction (positive USD181 million vs. negative USD69 million in January 2020).

Figure 1 – Spot FX flows (USD billion, 12M-to-date)



Sources: Brazilian Central Bank, Santander

Figure 2 – Net Spot FX flows (USD million, daily avg, sa)



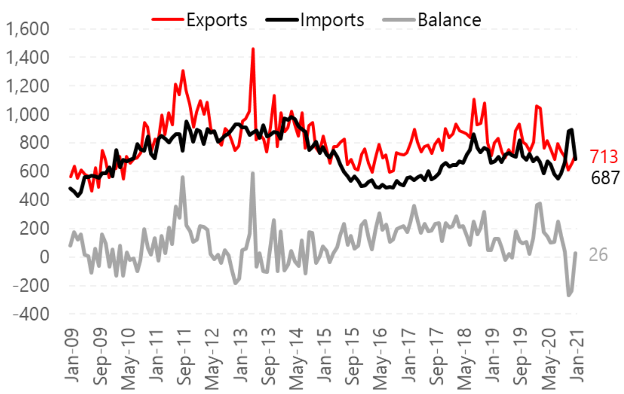
Sources: Brazilian Central Bank, Santander.

Taking a look at the behavior of the daily average flows of the different components of the spot FX market in seasonally adjusted terms, the anticipation of export proceeds outpaced the anticipation of import payments by a small margin; however, since we think the outlook for this year's trade balance is quite sanguine — commodity prices remain high; external demand has positive surprised us lately, etc. — we believe that trade flows should become more positive in the coming months, thus helping to partially curb pressure on the FX market. Regarding the financial segment, despite the negative outcome last month, the shortage seems to us a normal fluctuation after two months of positive results, and it was followed by the maintenance of relatively high inflows. That pattern may indicate some profit-taking spurred by Brazilian financials' favorable move at

YE2020. All in all, these data suggest to us more balanced results for the financial segment than those observed in 1H20.

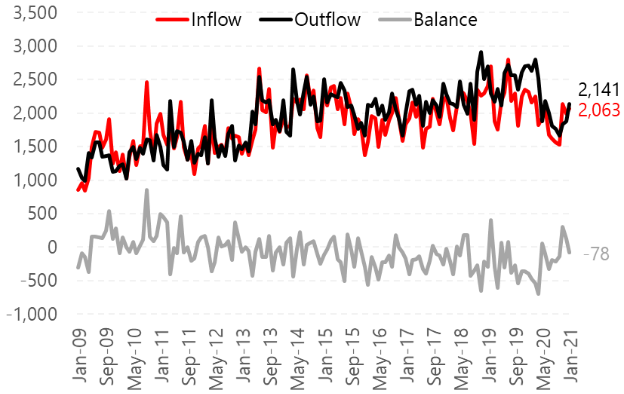
Adding to this more constructive view, we have the annualized balance of three-month moving averages in the commercial and financial segments, which indicated annual outflow of USD11.3 billion in January 2021, compared to an exit of USD87.4 billion in December 2019, which marked the historical low of the available time series. Therefore, at least for now, the spot FX flows do not hint at critical pressure on the BRL, in our view.

Figure 3 – Spot FX Flows – Commercial Segment (USD million, daily avg, s.a.)



Sources: Brazilian Central Bank, Santander.

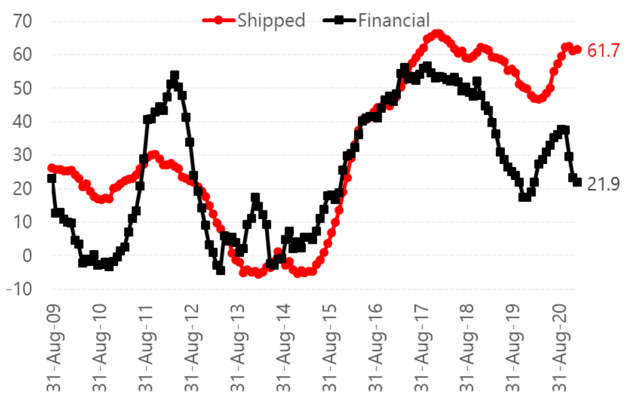
Figure 4 – Spot FX Flows – Financial Segment (USD million, daily avg, s.a.)



Sources: Brazilian Central Bank, Santander.

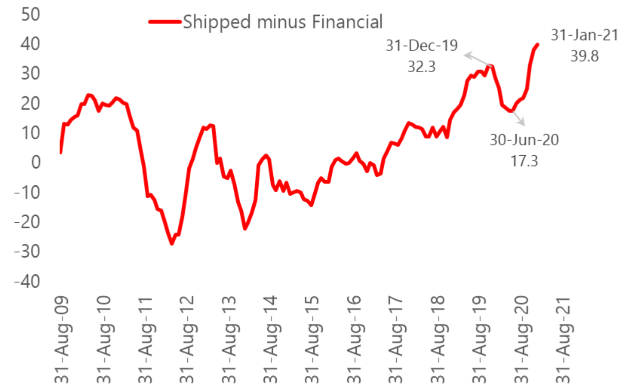
On top of the positive indications from the financial segment, we think that another factor related to the commercial segment is likely to help to ease pressures on the spot FX flow in the coming months. Unlike in the past — when Brazil faced an external debt crisis — exporters are currently allowed to keep their money outside the country in order to settle obligations or to invest their proceeds in other geographies. Thus, there may be a gap between the balance of "shipped goods" and their financial settlements. The following charts illustrate the current situation for that gap.

Figure 5 – Trade Balance: Shipped* vs Financial (USD billion, 12M-to-date)



Sources: Brazilian Central Bank, SECINT, Santander.
*Excluding oil platforms deals

Figure 6 – Gap Shipped* vs Financial (USD billion, 12M-to-date)



Sources: Brazilian Central Bank, SECINT, Santander.
*Excluding oil platforms deals

As one can note, although the Brazilian trade surplus has run at relatively high levels in 12M-to-date terms for the recent past, trade-related inflows have not registered a similar performance in the same period, which led the gap between the two to widen to a new historical breadth. Given the recent signal conveyed by the Brazilian Central Bank that monetary policy normalization is on the verge of beginning, along with the relatively weak level of the currency vis-à-vis its fundamentals, it seems us that exporters may be tempted to repatriate some of their money in the near future, in order to benefit from a wider interest rate differential than the current one, which may trigger a correction of the current level of the BRL.

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