Santander
Macroeconomic Research

BRAZIL MACRO

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DATA ANALYSIS – EXTERNAL SECTOR

IT HAS NOT BEEN POSITIVE ENOUGH

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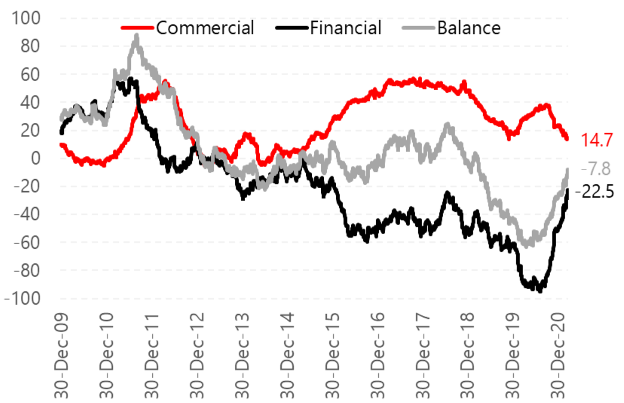
- **The Brazilian spot FX market recorded net inflows of USD1.6 billion in March 2021, leading to net inflows of USD8.7 billion during 1Q21. It is the first time since mid-2018 that the Brazilian spot FX market has registered a three-month streak of net inflows.**
- While the commercial segment saw net inflows last month (USD5.2 billion), the financial segment registered net outflows (USD3.7 billion) after having delivered positive results in the first two months of 2021. The combined results point to an improvement in the prospects for total spot flows in seasonally adjusted terms, although to a lesser degree than in previous months, in our view.
- **Nonetheless, the Brazilian Central Bank (BCB) carried out interventions in the spot FX market last month that amounted to USD3.6 billion—and some USD5.3 billion through FX swaps—which, indicate to us that the FX rate pressure has to do with elements other than external sector fundamentals.**

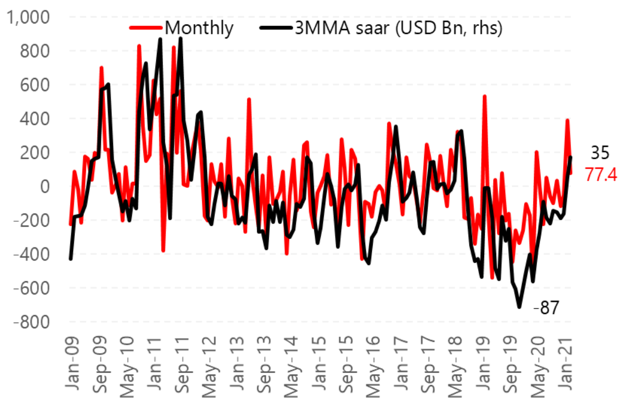
The Brazilian spot FX market recorded net inflows of USD1.6 billion in March 2021, as the commercial segment—which refers to trade-related flows—posted net inflows of USD5.2 billion in the period, while the financial segment recorded outflows of USD3.7 billion. Adjusting the data for the number of trading days, we find that the average net balance for the commercial segment was a positive USD228 million, which was below the year-ago level of USD377 million; financial average flows moved in the opposite direction (negative USD160 million vs. negative USD676 million in March 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)

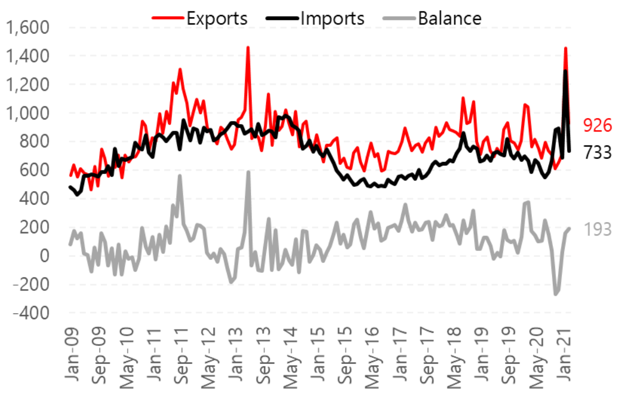


Sources: Brazilian Central Bank, Santander.

Taking a look at the seasonally adjusted daily average flows of the different components of the spot FX market during March, the anticipation of export proceeds continued to outpace the anticipation of import payments, but by a larger margin than in previous months. The outlook for the trade balance this year is quite favorable—commodity prices remain high and external demand has positively surprised us lately, among other factors. As a result, we believe trade flows should become even more positive in the coming months, thus helping to eventually curb pressure on the FX market. Regarding the financial segment, the data from March supports our perception that the segment should remain balanced in the coming months, absent negative surprises on the domestic fiscal front.

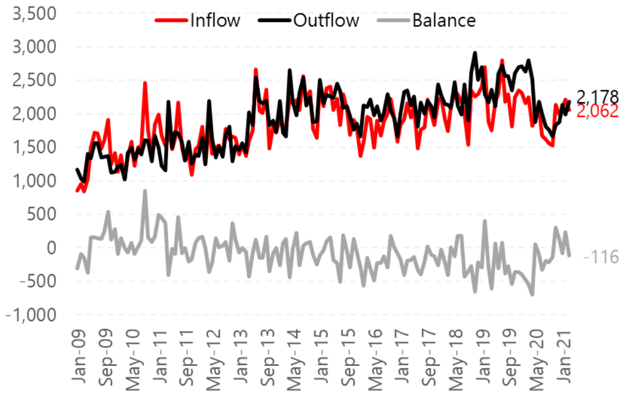
Additional data supports our constructive view: the annualized balance of three-month moving averages in the commercial and financial segments indicated annual inflows of USD35.0 billion in March 2021 compared to outflows of USD87.4 billion in December 2019, which marked the historical low of the available time series. Therefore, spot FX flows currently do not suggest critical pressure on the BRL, in our view, although we note recent data points are less supportive. However, the BCB needed to intervene heavily in the spot FX market last month when it provided USD3.6 billion to market participants in order to soften the weakening of the USD/BRL, which reached as high as 5.87 on an intraday basis. The move reinforces our perception that other factors are weighing on the BRL's dynamics.

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



Sources: Brazilian Central Bank, Santander.

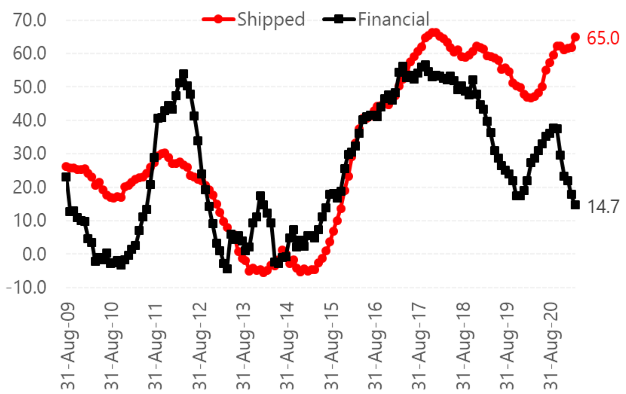
Figure 4: Spot FX Flows – Financial Segment (USD million, daily avg, s.a.)



Sources: Brazilian Central Bank, Santander.

Although the Brazilian trade surplus has remained relatively high on a 12-month-to-date basis, trade-related inflows have not registered a similar performance, which has led the gap between the balance of "shipped goods' and their financial settlements to widen to a new historical level. Exporters may feel more tempted to repatriate some of their money in the near future, in our view, because of the relatively weak level of the currency vis-à-vis fundamentals, and in particular, as the common view is that monetary policy normalization is quite likely to continue in the coming months.

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



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

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

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

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