BRAZIL MACRO

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DATA ANALYSIS – EXTERNAL SECTOR

THE GAME GOES ON

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- Although the USD7.3 billion deficit registered by the Brazilian current account in January 2021 exceeded our expectation (USD6.9 billion deficit), it has continued to shrink in 12-month-to-date terms, thus keeping us comfortable with the expected trajectory for further improvement in the coming months.
- The volume of direct investments in the country last month also fell short of our expectation (USD1.8 billion versus USD3.5 billion), but its descending trend in 12-month-to-date terms seems to us to be pointing toward a U-turn soon. That is, the outlook for Brazilian external financing needs remains favorable, in our opinion.
- In addition, foreign investors have continued to be net buyers of Brazilian financial assets in the domestic market for the eighth month in a row, which indicates that some of the ample international liquidity has favored the country, in our view.
- Once again, we think today's data add to the set of signals that BRL weakness is related to something other than the fundamentals of the Brazilian balance of payments.

Higher Now, Lower Later

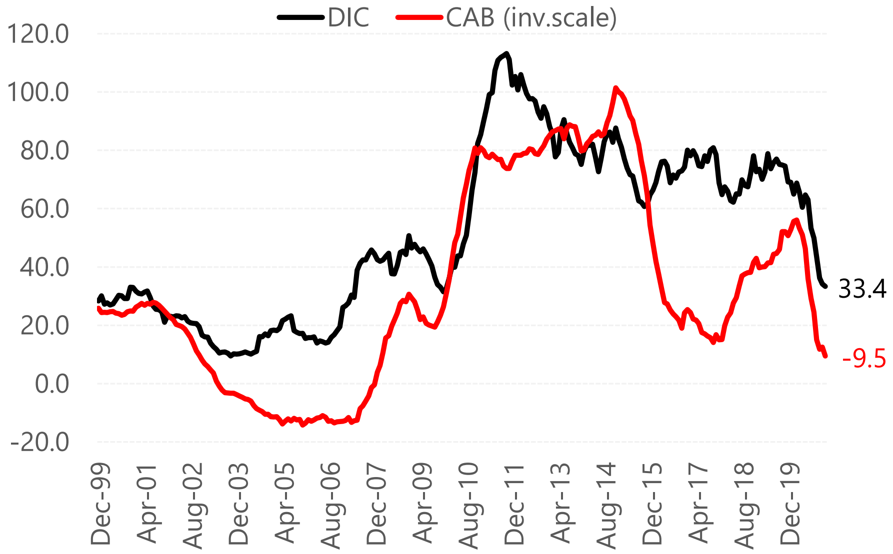
The Brazilian current account balance registered a USD7.3 billion deficit in January 2021, which was a little above our estimate of a USD6.9 billion deficit for the period, due to larger interest payments than indicated by the schedule provided by the BCB. Despite the setback, the result did not alter the trajectory of improvement that the current account balance has shown in 12-month-to-date terms since March 2020, when it reached a deficit of USD56.1 billion compared with a deficit of USD9.5 billion last month in these terms. Moreover, as the volume of interest paid is higher now, we think it is reasonable to expect that these outlays will be lower in the future, thus causing a simple dislocation of the current account balance during the year, but not affecting its final result – we project it to reach a USD17.6 billion surplus this year.

Despite these larger interest payments, it is important to note that the remittance of profit and dividends remained quite subdued (USD0.8 billion compared with USD1.5 billion a year ago), which seems to us additional evidence that the deficit in the primary income account should be similar to the one observed last year, based on the combination of a gradual economic recovery in Brazil and a weaker-than-expected level for the exchange rate as well. Another item that in the past was a source of sizeable expenditures has also shown a small imbalance, namely tourism outlays. We believe that mobility restrictions are probably playing a role in this contraction, but we think one cannot rule out some impact from the weak currency too. Since we do not expect the BRL to show substantial strengthening in the coming months (details in the link[1]), we also believe that the services account is not likely to register a major deterioration ahead. Therefore, it seems to us that the trade balance should be the main driver for the behavior of the current account balance this year. However, it

[1] **Santander Brazil - Macroeconomic Scenario:** ***"The Persistence of (Fiscal) Risks"* –** February 11, 2021- Available on: http://bit.ly/Sant-ScenRev-fev21

is important to bear in mind that last month there were imports of oil platforms, which is an *ad hoc* factor that we think requires us to react to the trade deficit observed in the period with a pinch of salt (details in the link[2]).

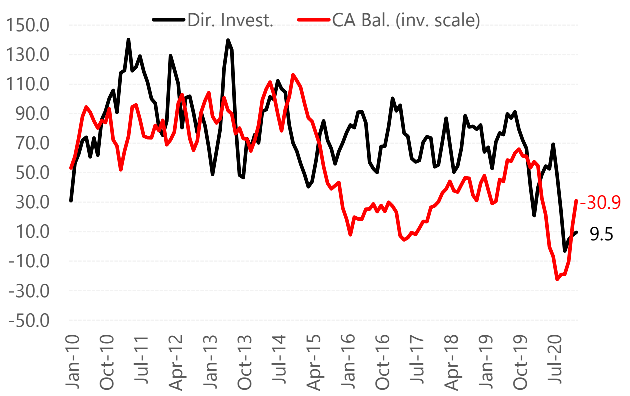
Figure 1 – Current Account Balance vs. Direct Investments in the Country (USD billion)



Sources: Brazilian Central Bank, Santander.

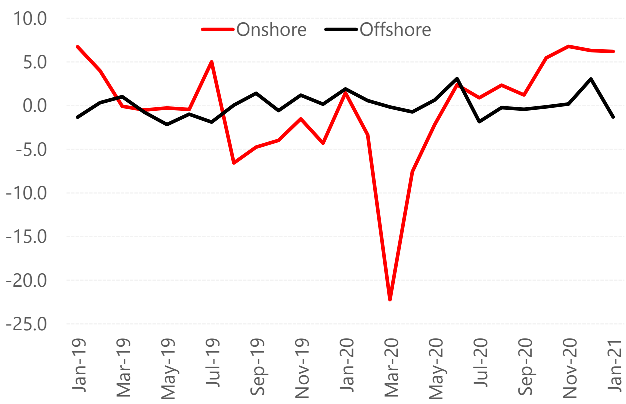
Taking a look at the financial account, the volume of direct investment in the country (DIC) also frustrated our expectation, as it was nearly half of what we estimated for last month (USD1.8 billion versus USD3.5 billion), which also kept its 12-month-to-date trajectory in a downward trend, although less steeply than the one presented by the current account deficit. That is, we continue to see quite comfortable conditions for the Brazilian external financing needs to be met this year. Moreover, according to preliminary figures from the BCB, we are about to see a U-turn in this trend in February 2021 – a move that is also indicated by the 3MMA-saar figures of the DIC. We acknowledge that the 3MMA-saar figures of the current account balance and DIC have pointed to some deterioration in that relationship, but it is important to bear in mind that the former was affected by the distortion caused by the import of oil platforms.

Figure 2 – Current Account Balance vs. Direct Investment in the Country (USD billion, 3MMA-saar)



Sources: Brazilian Central Bank, Santander.

Figure 3 – Net Foreign Portfolio Investments (US$ billion, monthly flows)



Sources: Brazilian Central Bank, Santander.

Another development that has also brought some good news with respect to the dynamics of the financial account was foreign portfolio flows directed to the acquisition of Brazilian assets in the domestic market, as that number registered the eighth positive reading in a row in January 2021 (USD6.2 billion). In sum, the global liquidity conditions are there and continue to help the country maintain the sound fundamentals of its balance of payments, in our view.

[2] **Santander Brazil External Sector - *"(Partially) Sunk by platforms"* –** February 01, 2021- Available on: http://bit.ly/Sant-ext-sec-010221

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