

FINANCIAL CONDITIONS INDEX AT SIX-MONTH HIGH**Gabriel Couto***
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- **Our financial conditions indicator (FCI) for September (with data up to September 25) showed additional tightening, with the second increase in a row. The index remains in restrictive territory (positive values = restrictive position).** After showing some easing throughout 2Q23, the index (always presented on a scaled basis) has returned to levels close to YE2022. In September, the index has tightened by 0.20 points, to 1.07 points (from 0.87 points in August), and has reached its highest level since March.
- **Zooming in on the details, the breakdown indicates that most components contributed to September's increase.** Both foreign (+0.10 p.p.) and domestic (+0.10 p.p.) factors contributed positively to the index. Most of the components pointed to tightening conditions. Oil prices (+0.11 p.p.), currencies (+0.06 p.p.) and foreign rates (+0.03 p.p.) were the highlights of the tightening conditions. Commodities (+0.02 p.p.) and domestic rates (+0.01 p.p.) also contributed positively to the index (i.e., contributed to tightening). Conversely, risk (-0.03 p.p.) helped to ease financial conditions, as capital markets (0.00 p.p.) had neutral contribution. When we exclude oil prices from the analysis, we see a 0.09 p.p. increase in the FCI (ex-oil), to 1.04 p.p. (vs. 0.96 p.p. in August). At the margin, we continue to see domestic factors contributing more to the easing of the FCI, while foreign factors remain at restrictive levels.
- **The September's FCI update slightly increases the predicted recession probability for December, and that probability remains above the false-positive threshold.** In December-June, our recession tracker (based on a three-month lagged FCI) reached virtually the same levels seen during the worst periods of Brazil's 2014-16 recession and is again close to these levels, following the recent tightening seen in the FCI.
- **Our 3Q23 GDP growth tracking stands at -0.3% QoQ-sa, and our forecast for full-year 2023 growth is +2.5%.** Despite the recent positive surprise in 2Q23 GDP result, we continue to see signs of deceleration for broad activity ahead, especially for more cyclical segments, owing to highly restrictive financial conditions. In addition, we expect negative contributions from farm output for 2H23, as the positive impact of the record summer crops was limited to 1Q23 and the beginning of 2Q23.

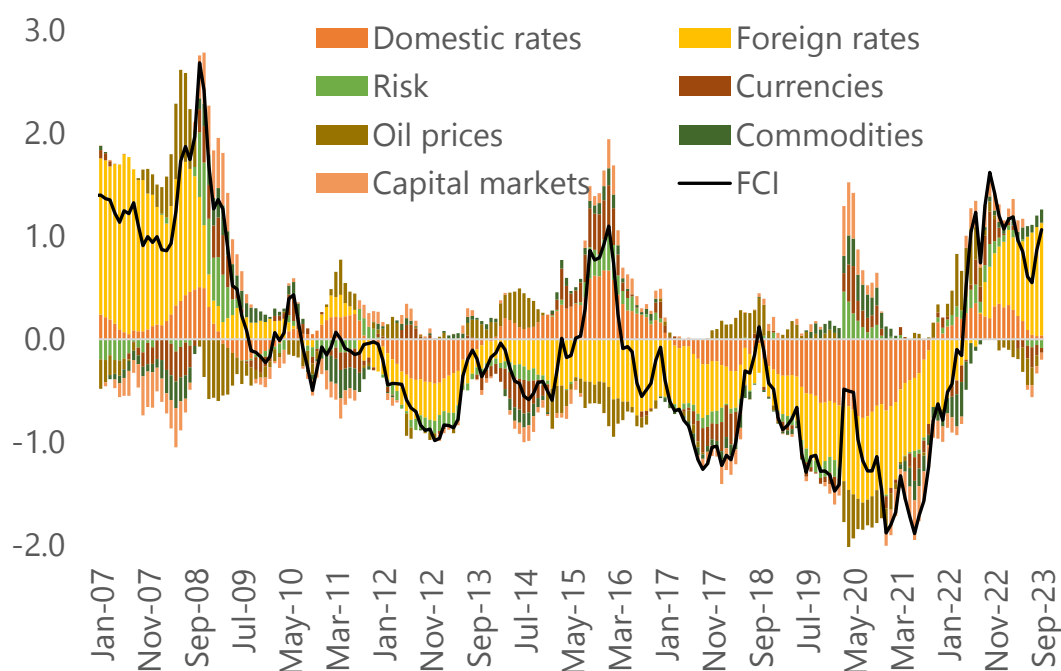


Figure 1 – Santander's FCI Breakdown

Financial Conditions Indicator							
	Weights	Headline				Change	
		Jul-23	Aug-23	Sep-23		Aug-23	Sep-23
FCI	100%	0.55	0.87	1.07	↑	0.32	0.20
Domestic rates	34%	0.04	0.03	0.04	→	-0.01	0.01
Foreign rates	33%	1.00	1.06	1.09	↑	0.07	0.03
Risk	18%	-0.08	-0.06	-0.08	↓	0.02	-0.03
Currencies	20%	-0.19	-0.10	-0.05	↑	0.09	0.06
Oil prices	23%	-0.18	-0.10	0.00	↑	0.07	0.11
Commodities	-13%	0.07	0.11	0.13	↑	0.04	0.02
Capital markets	-15%	-0.11	-0.07	-0.07	→	0.04	0.00
FCI (ex Oil)	-	0.72	0.96	1.04	↑	0.24	0.09
Domestic Factors	-	-0.32	-0.23	-0.13	↑	0.08	0.10
Foreign Factors	-	0.87	1.10	1.20	↑	0.24	0.10

Sources: Bloomberg, BCB, Santander.

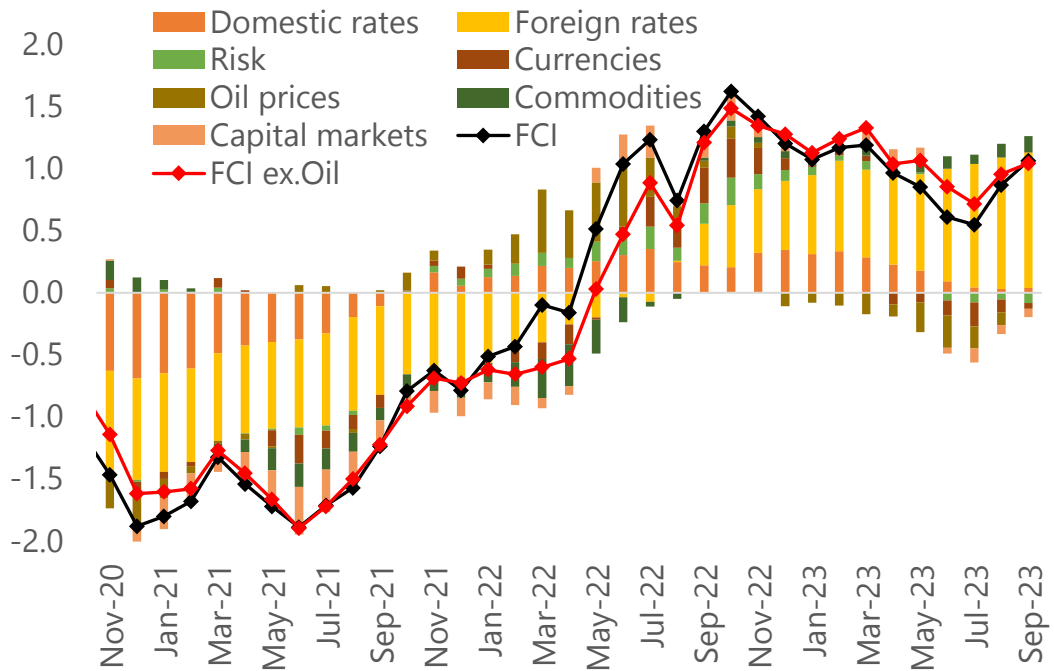
Figure 2 – Santander's FCI Proxy (from 2007 to 2023)



Sources: Bloomberg, BCB, FGV, Santander.

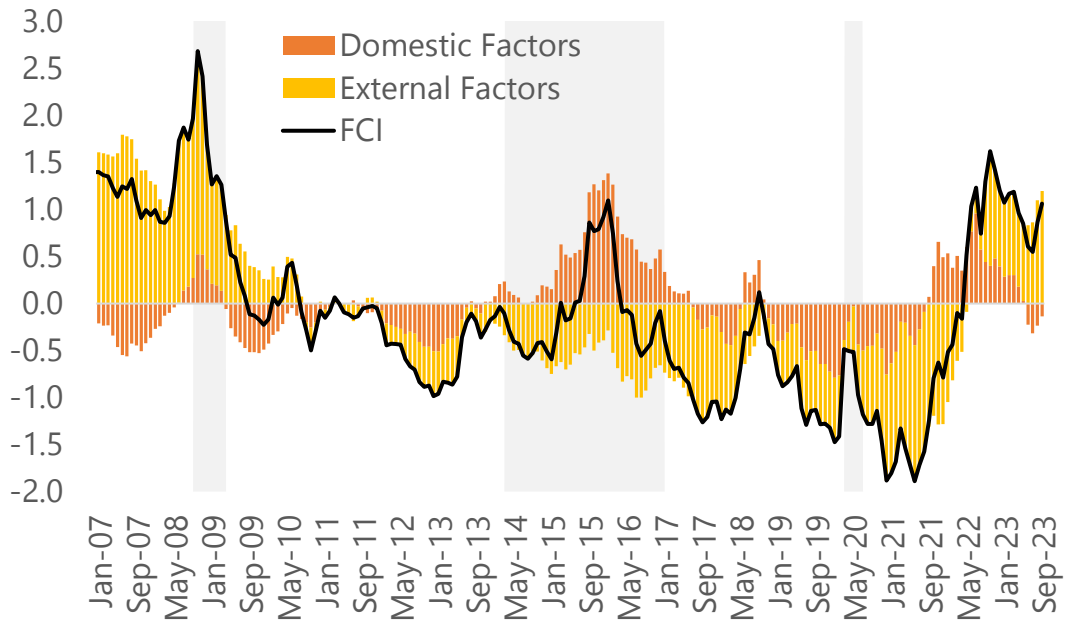


Figure 3 – Santander’s FCI Proxy (from 2020 to 2023)



Sources: Bloomberg, BCB, FGV, Santander.

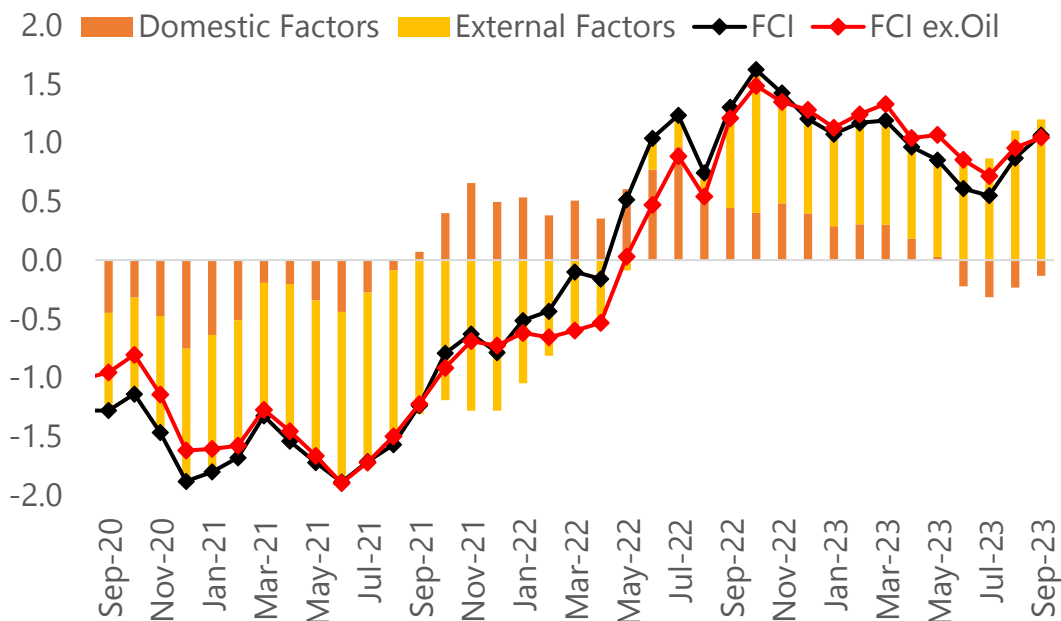
Figure 4 – Santander’s FCI Proxy Breakdown (from 2006 to 2023)



Sources: Bloomberg, BCB, FGV, Santander.

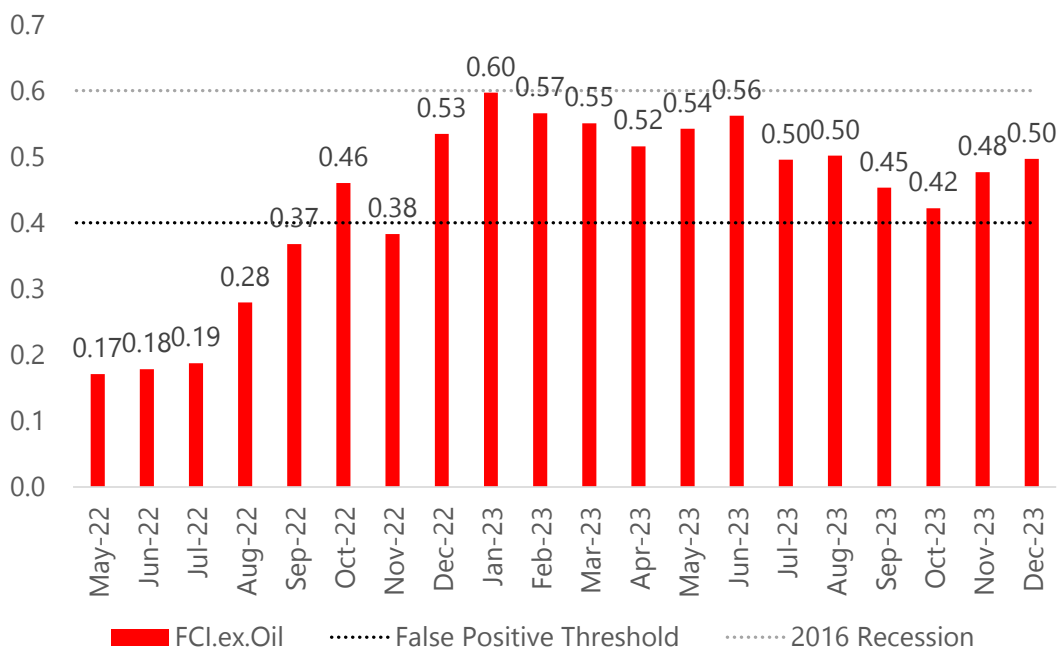


Figure 5 – Santander’s FCI Proxy Breakdown (from 2020 to 2023)



Sources: Bloomberg, BCB, FGV, Santander.

Figure 6 – Recession Probability Tracker Based on FCI (2022 to 2023)



Sources: Bloomberg, BCB, FGV, Santander.

For details on Santander’s economic activity outlook, please refer to our last reports¹.

¹ **Santander Brazil Economic Activity: “Upgrading Our 2023 GDP Growth Forecast (Again)”** – September 22, 2023 – Available on: [Std-chart-econact-sep23https://tinyurl.com/Std-chart-econact-sep23](https://tinyurl.com/Std-chart-econact-sep23)



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