BRAZIL MACRO

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GDP PREVIEW

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Tepid GDP Growth Expected in 3Q21

- **We expect a tepid GDP growth in 3Q21 (+0.1% QoQ-sa).** September's release of IBC-Br capped a 3Q21 that was not as strong as previously thought and the quarterly results highlighted the ambiguity between solid services spending and a weak demand for goods, as part of the reopening and "post-pandemic" normalization process. We lowered our 3Q21 projection to +0.1% QoQ-sa (from +0.2%), with this positive figure reflecting our expectations of good GDP contributions from segments that are still expected to profit on the reopening and that are usually not well captured by timely indexes.
- **On the supply side, we expect continued rebound of the services sector (+0.7%), as the health crisis subsides and mobility returns to "normal".** On the other hand, industry should weight on activity (-1.0%), reflecting continued weakening of manufacturing reinforced by weak figures seen in mining and construction. Moreover, we expect farm output to continue to weaken (-0.5%), partially giving back the solid 1Q21 contribution.
- **On the demand side, we expect healthy growth for household consumption (+0.6%).** Even considering the ambiguity between services and goods spending, the steep climb seen in the services to families segment should boost household consumption in 3Q21. Conversely, investment should retreat at the margin (-0.9%), stemming mainly from weak figures of domestic capital goods production.
- **If our projection is met, this result would imply a carryover of 4.9% to 2021.** Moreover, it would place the economy at the same levels seen in the pre-pandemic mark (4Q19) for the second quarter in a row, highlighting a loss of steam of overall output during this "post-pandemic" normalization process.
- It is worth noting that IBGE usually publishes important revisions in the historical GDP series in its 3Q21 release. It is not an easy task to anticipate such movements, so we do not take any specific view about these potential revisions.

Figure 1. GDP Projections Breakdown*

	2Q21		3Q21e		Rolling 4Q	4Q19*
	% YoY	% QoQ	% YoY	% QoQ	%	%
GDP	12.4	-0.1	4.4	0.1	3.9	0.0
Supply						
Taxes	16.8	-0.7	5.0	-0.2	5.5	-4.5
Agriculture	1.3	-2.8	0.1	-0.5	1.9	2.7
Industry	17.8	-0.2	-0.1	-1.0	4.9	0.6
Mining	7.0	5.3	2.6	-1.0	0.4	-0.1
Manufacturing	25.9	-2.2	-0.7	-1.2	7.9	0.9
Construction	13.1	2.7	5.0	-0.2	2.8	0.4
Utilities	6.7	-0.9	-1.6	0.0	2.1	1.4
Services	10.8	0.7	6.5	0.7	3.3	-0.2
Demand						
Consumption	10.8	0.0	3.9	0.6	2.4	-0.7
Government	4.2	0.7	2.5	0.6	-0.7	-4.9
Investments*	32.9	-3.6	18.0	-0.9	19.9	37.8
Exports	14.1	9.4	3.3	-11.2	3.6	14.2
Imports	20.2	-0.6	25.4	-5.3	11.5	18.2

Sources: IBGE, Santander estimates. * We set up our pre-crisis mark at 4Q19

Activity indexes releases highlighted a 3Q21 not as strong as previously thought. September's release of IBC-Br capped a 3Q21 summarizing the tepid figures seen for economic activity, with the broad activity index posting a slight quarterly decline (-0.1% QoQ-sa). The quarterly results highlighted the ambiguity between solid services spending and a weak demand for goods, as part of the reopening and "post-pandemic" normalization process of household consumption and in opposition with the pattern seen throughout 2H20. This last batch of weak figures motivated us to lower our 3Q21 projection to +0.1% QoQ-sa (from +0.2%), highlighting a loss of steam of economic activity amid this "post-pandemic" normalization process, but we still expect a positive figure, reflecting our expectations of good GDP contributions form segments that are still expected to profit on the reopening and that are usually not well captured by timely indexes period (e.g., other services and public services).

We expect the heterogenic composition of overall GDP seen in 2Q21 to be repeated in 3Q21 release. On the supply side, we expect continued rebound of the services sector (+0.7%), as the health crisis subsides and mobility returns to "normal". We expect good growth contribution coming from services segments that still show wide idleness compared to the pre-crisis period (e.g., other services and public services, that account for 30% of total GDP). Indeed, the services to families segment of IBGE's monthly survey (which captures bars, restaurants, leisure activities and other mobility-related activities) highly correlates with these idled segments and expanded 17.2% in 3Q21 (+4.2% in 2Q21), which can be a source of positive surprise to our 0.7% GDP services growth projection. Conversely, industry should weight on activity (-1.0%), reflecting continued weakening of manufacturing (-1.2%) but reinforced by weak figures expected for mining (-1.0%) and construction (-0.2%). This pattern is in opposition to the one seen last quarters, when construction and mining cushioned manufacturing's tumble impact. In addition to the ambiguity seen in services and goods-related sector, we expect farm output to continue to weaken (-0.5%), partially giving back its solid 1Q21 contribution, albeit we see relevant downside risks to this projection amid September's weaker figures for livestock output.

On the demand side, we expect household consumption to climb (+0.6%). Even considering the ambiguity between services and goods in household's spending, the steep climb seen in the services to families segment should boost private consumption in 3Q21. Indeed, as described above, the services to families' real revenue climbed 17.2% in 3Q21 (+4.2% in 2Q21) and we expect this growth to offset the quarterly retreat seen in broad retail sales (-1.7%). We expect government consumption to expand 0.6%, as the provision of public services (such as non-mercantile health and education services) gradually recovers. The external sector should contribute negatively, reflecting weak exports (-11.2%) not fully offsetting the plummet in imports (-5.3%). It is worth saying that, in stark contrast to the 2Q21 release, when the proxy of inventories replenishment dragged down GDP (-1.8% contribution, according to our calculations), our 2Q21 forecast is consistent with a positive contribution from inventories (+1.4%) on the final result.

If our projection is met, this result would imply a carryover of 4.9% to 2021. Moreover, it would place the economy at the same levels seen in the pre-pandemic mark (4Q19) for the second quarter in a row, highlighting a loss of steam of overall output during this "post-pandemic" normalization process. In terms of outlook, we expect the services to sector to continue to contribute to sequential growths in the coming quarters. Indeed, some segments of the services sector (transport, other services and public services) will still be running at depressed levels, and their recovery could take place after vaccination advances, mobility returns to "normal" and the health crisis ebbs. It is worth noting that IBGE usually publishes important revisions in the historical GDP series in its 3Q21 release. It is not an easy task to anticipate such movements, so we do not take any specific view about these potential revisions. **For details on Santander's activity outlook, please refer to our last chartbooks[1].**

[1] **Santander Brazil Economic Activity -** ***"Chartbook – Downgrading the Estimate for 2022 and 2023"*** **–** November 05, 2021 – Available on: https://bit.ly/Std-chart-econact-nov21
Santander Brazil Economic Activity - ***"Chartbook – Household Indebtedness Expected to Slow Lending in 2022"*** **–** November 09, 2021 – Available on: https://bit.ly/Std-chart-credit-nov21

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