MACRO BRAZIL

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DATA ANALYSIS – BALANCE OF PAYMENTS

A (VERY) POSITIVE SURPRISE

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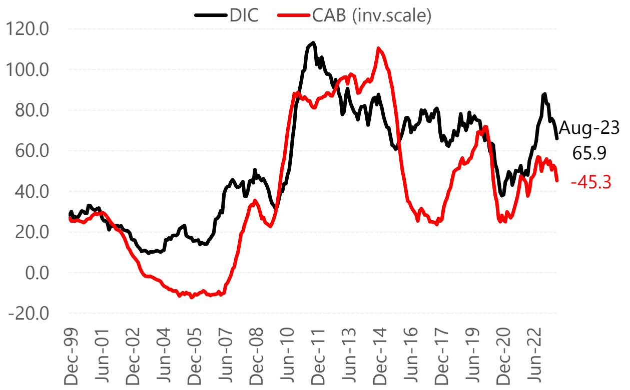
- **Today, the Brazilian Central Bank (BCB) released August balance-of-payments (BoP) data, which revealed a monthly current account deficit of USD0.8 billion, a figure better than our estimate of a USD2.7 billion deficit and the market median projection (-USD1.8 billion). The figure was also far below the one registered a year ago (-USD7.0 billion). As a result, the 12-month current account deficit receded to USD45.3 billion from USD51.6 billion in July's release, thus remaining below the USD53.6 billion deficit reported at the end of 2022. That is, the current account balance continued to improve this year, a trend that was reinforced by its 3MMA-saar gauge, which reached -USD23.8 billion vs. -USD72.2 billion at the end of last year.**
- **Lower-than-expected remittances of profits and dividends and smaller-than-anticipated services outlays accounted for the bulk of the difference between our estimate and the actual result, while trade figures were relatively in line with our calculations. August was the first month of 2023 in which the remittances of profits and dividends fell significantly short of the figures observed in the same period of the previous year, which reinforces our view that economic activity is slowing.**
- **Regarding the components of the financial account, the volume of direct investments in the country fell to USD4.3 billion last month, a reading lower than we projected (USD5.3 billion). The figure was also worse than a year ago (USD10.0 billion), leading 12-month rolling volume to recede to USD65.9 billion in August vs. USD71.7 billion in July. In other words, despite the negative surprise, the country continued to comfortably meet its external financing needs. The setback was related to the amortization of intercompany loans, which we think reflects a stronger BRL fostering the anticipation of these payments.**
- **Regarding portfolio operations, foreigners were net sellers of assets in the domestic market (USD0.8 billion) in August, thus extending the sales reported in July (USD0.3 billion). However, sales this time were focused on the equity market (USD2.2 billion), whereas there were some purchases of assets in the bond market (USD1.5 billion). This backdrop reinforces the importance of the interest rate differential to portfolio flows, in our view.**
- **All in all, we think that August BoP data is unlikely to affect the generally constructive view of the external position of the Brazilian economy, as the current account deficit is running at manageable levels, and the financial account has a favorable outlook.**

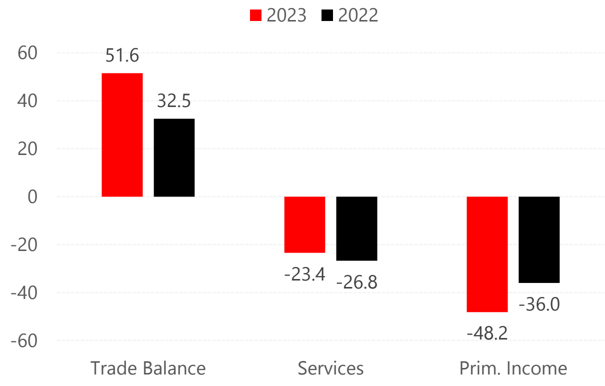
The release of Brazilian balance-of-payments data for August showed the current account balance with a deficit of USD0.8 billion rather than the USD2.7 billion deficit we expected to see. Besides coming in better than our expectation, the deficit fell far short of the one reported a year ago (-USD7.0 billion), which led the current account gap to recede to USD45.3 billion in 12-month terms (or -2.2% of GDP). Part of the difference vs. our estimate was related to smaller remittances of profits and dividends than we had calculated, as, for the first time in 2023, these items came in substantially lower than the volume reported a year ago. We think this may be an indication that the economy is losing steam, as we expected on the heels of the lagged effects of the prior interest rate hikes. Another part of the surprise stemmed from lower-than-anticipated outlays for services, which we also see as a signal that the Brazilian economy is slowing. These positive surprises were accompanied by foreign trade data relatively in line with our expectation.

Figure 1. Current Account vs. Direct Investment (USD billion, 12m)



Sources: Brazilian Central Bank, Santander.

Figure 2. Current Account Balance – Selected Items (USD billion, Jan-Aug)

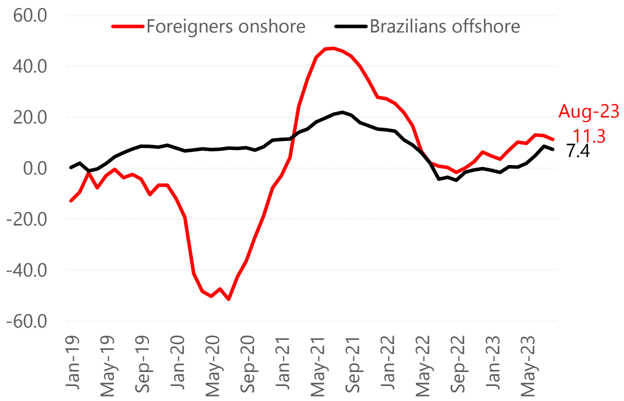


Sources: Brazilian Central Bank, Santander.

The current account deficit reached USD19.5 billion in year-to-date terms in August 2023 compared with a USD27.7 billion deficit in the same terms in August 2022. Looking at its components, we noted that they followed different paths, with the deficit in the primary income account — which comprises interest payments and remittances of profits and dividends — reaching USD48.2 billion this year vs. USD36 billion in 2022, which we believe has to do with concerns about changes in tax rules and a stronger BRL. On the other hand, the deficit in the services account receded to USD23.5 billion in 2023 vs. USD26.8 billion last year, as the economy has lost steam of late — and we believe it will continue to do so in the coming months. Finally, the trade surplus climbed to USD51.6 billion in 2023 vs. USD32.5 billion last year on the heels of a strong decline in import outlays (to USD176.8 billion from USD194.6 billion) and relatively stable export revenue (USD228.4 billion vs. USD227.1 billion). While both export and import prices have retreated during 2023, export volume has outpaced import volume, opening room for this sizeable trade surplus. These dynamics suggest that we could see a smaller current account deficit for 2023 than the USD53.3 billion we forecast currently.

Regarding the financial account, direct investments in the country fell short of our estimate (at USD4.3 billion vs. USD5.3 billion in our forecast), but still indicating that the most reliable source of external funding could continue to fill the current account gap over the medium term. On the other hand, portfolio investments have lost steam lately, with foreigners being net sellers of Brazilian financial assets in the domestic market for the second month in a row. This time, the bulk of the sales were of equity instruments (-USD2.2 billion), as there were net purchases of USD1.5 billion in the bond market, which we believe to be related to a still attractive interest rate differential. As we expect the economy to lose further steam and the domestic interest rate to come down, these portfolio flows will likely continue to retreat, thus reinforcing our view that there is limited room for the BRL to strengthen ahead.

Figure 3. Portfolio Investments – Selected Items (USD billion, 12m)



Sources: Brazilian Central Bank, Santander.

All in all, we think the data indicates that the Brazilian economy continues to be in a comfortable situation regarding its external sources of funding, which we expect will keep the Brazilian balance of payments off the radar of market concerns.

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