

## BIGGER BUT MANAGEABLE

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- Yesterday the Brazilian Central Bank (BCB) released August and September balance-of-payment (BoP) data, which revealed current account deficits of US\$5.4 billion and US\$5.7 billion, respectively, for the latter. Both figures came in worse than our estimates of US\$2.9 billion deficits for both months, thus leading to a current account deficit of US\$46.2 billion in 12-month terms (~2.6% of GDP).
- Negative surprises in both results stemmed from much larger remittances of profits and dividends than we anticipated, as trade balance surpluses and services income deficits in the period were in line with our expectations. As a result, the 3MMA-saar gauge for the current account deficit worsened to US\$60.7 billion in September from US\$36.8 billion in July, which undermines confidence in our expectation of a US\$39.1 billion deficit for FY2022.
- Contrasting with these unfavorable outcomes in the current account balance (CAB), we continued to see sizeable investment flows into the country. The volume of direct investments in the country (DIITC) was US\$18.0 billion in the two months, which led to a US\$73.8 billion amount in 12-month terms (the highest level since end 2019). Therefore, Brazil continues to be in a comfortable situation as far as external financing is concerned.
- Despite the relatively soothing backdrop described above, we highlight that foreign portfolio investments in the domestic market registered mixed results in August and September, with inflows in the fixed income segment being accompanied by outflows in the equity market. At the same time, we saw Brazilian portfolio investments abroad being unwound, which indicates a greater appetite to keep money in the country, in our opinion.
- All in all, given the still manageable level of the current account deficit and the favorable prospects regarding the financial account, we think the constructive view of the Brazilian external position is likely to continue offering partial insulation against international jitters.

The release of the (delayed) figures for Brazilian balance-of-payments data for August and September showed a deterioration in the current account deficit in 12-month terms, to US\$46.2 billion. The bulk of the worsening in the current account deficit is associated with larger remittances of profits and dividends stemming from stronger-than-expected economic activity in 1H22 on the heels of fiscal incentives and the normalization of activities that were previously hit by the COVID-19 pandemic, as well as an anticipation to potential changes in the taxation over dividends from 2023 onwards. Consequently, we saw the actual monthly figures (-US\$5.4 billion and -US\$5.7 billion, respectively) revealing worse performance than our estimates (-US\$2.9 billion for both months). We expect smaller remittances of profits and dividends ahead as the lagged effects of prior interest rate hikes start to take a toll on economic activity in the coming months. That is, we continue to see remittances as an endogenous mechanism of adjustment that currently characterizes the current account balance.

The deterioration in the current account dynamics was also pointed out by the behavior of the 3MMA-saar gauge, which climbed to US\$60.7 billion (3.4% of GDP) from US\$36.6 billion (2.1% of GDP) in the previous release. This level is much higher than our forecast of US\$39.1 billion for FY2022 and the last quarter of each year bears unfavorable seasonal influences to current account balances, which undermines the probability of our forecast to materialize.

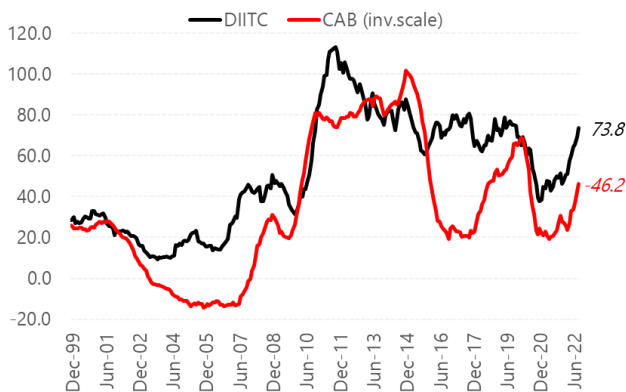
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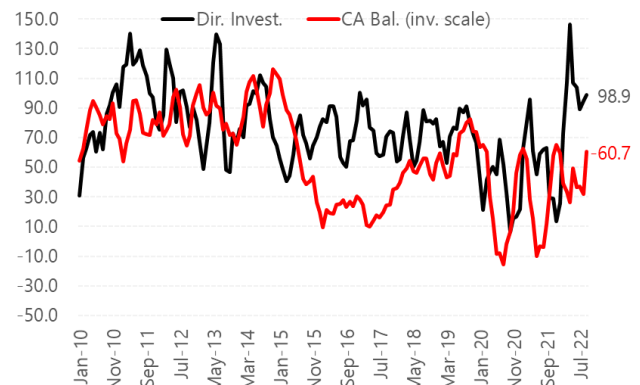


**Figure 1. Current Account Balance vs. Direct Investment in the Country (USD billion, 12m)**



Sources: Brazilian Central Bank, Santander.

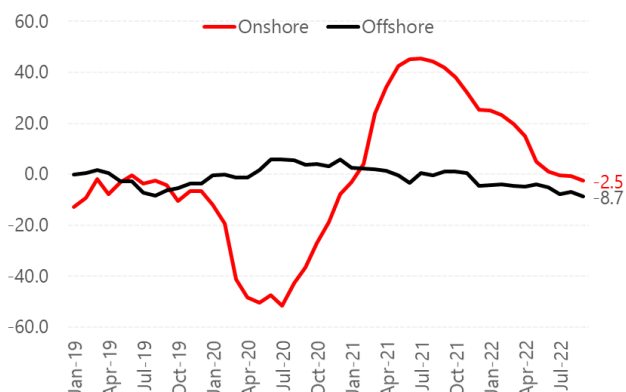
**Figure 2. Current Account Balance vs. Direct Investment in the Country (USD billion, 3MMA-saar)**



Sources: Brazilian Central Bank, Santander.

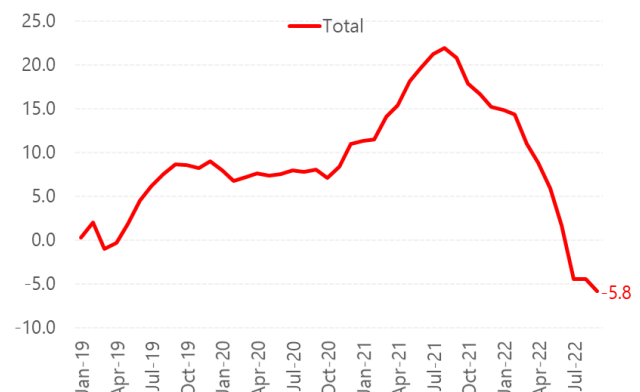
However, we believe the deterioration in the current account balance does not imply a negative trend for the future, especially when we consider that direct investments in the country have continued to flow fairly freely. Given the US\$18.0 billion recorded during August and September, the amount amassed in 12-month terms reached US\$73.8 billion, which is the highest level observed since year end 2019. If we look at the 3MMA-saar gauge, the picture is comfortable as well, as it points to a somewhat higher level than the one shown by the current account deficit on the same terms. In sum, the Brazilian economy continues to be in a comfortable situation regarding its external source of funding, which we expect to keep the Brazilian balance of payments off the radar of market concerns.

**Figure 3. Net Foreign Portfolio Investments (USD billion, 12-month)**



Sources: Brazilian Central Bank, Santander.

**Figure 4. Brazilian Portfolio Investments Abroad (USD billion, 12-month)**



Sources: Brazilian Central Bank, Santander.

Although the funding of the current account deficit is an undemanding task, in our view, and the backdrop for the Brazilian balance of payments does not cause significant worries, we highlight that the volume of foreign portfolio investments in the domestic market registered a mixed outlook in August and September, with net inflows in the former and net outflows in the latter. As a result, we continued to see a declining trend in 12-month terms. In our view, this is a sign of foreigners' caution regarding the price dynamics of Brazilian financial assets in the coming months, especially amid lingering uncertainties regarding the future of economic policy from 2023 onward. In turn, Brazilian portfolio investments abroad continued to move into negative territory in 12-month terms, which indicates the repatriation of money to the country, thus partially offsetting foreigners' withdrawals. That bodes well for the maintenance of positive results in the financial account in the near future, but we see a limited capacity for the repatriation process to offset larger (or more protracted) foreign outflows. Therefore, although the constructive view of the Brazilian external position is unlikely to be changed by today's figures, we believe a stronger BRL will require structural improvements in other segments of the Brazilian economy.



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