BRAZIL MACRO

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DATA ANALYSIS – FISCAL POLICY

POSITIVE PRIMARY RESULT DRIVEN BY REGIONAL GOVERNMENTS

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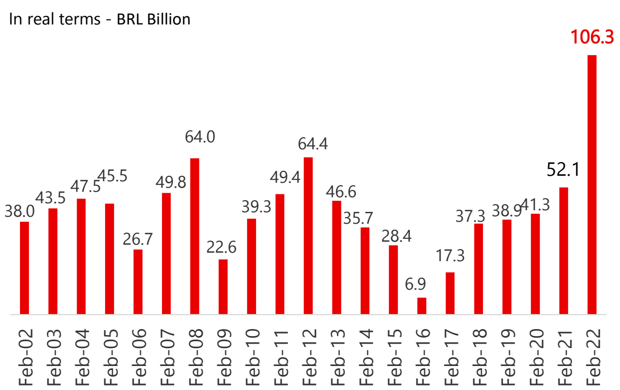
- Today, the BCB unveiled the consolidated public sector's fiscal balance for February (previously scheduled for release March 31), thanks to a pause in the federal workers' strike. In February, the public sector posted a primary surplus of BRL3.5 billion, significantly better than our forecast (-BRL8.6 billion) and the market's median estimate (-BRL8.3 billion). This was the best result for the month in the historical series. The main surprise (again) came in the regional governments' result, which was a surplus of BRL20.2 billion, higher than our call (BRL12.4 billion).
- According to the data published by the Treasury on March 24, the central government posted a primary deficit of BRL20.6 billion in February. Expenditures rose 6.5% YoY in real terms, with a higher-than-expected increase in heath expenditures. Revenue rose 14.8% YoY, favored by extraordinary oil-related Transfer of Rights revenue (BRL11.2 billion). For 2022, our forecast points to a central government deficit of BRL45 billion (0.5% of GDP), based on an increase in expenditures and some softening in revenue growth in 2H22.
- We forecast a balanced public sector result in 2022, considering an increase in expenditures and some softening in revenue growth—although a more lasting price shock effect on revenue could add a positive bias to the deficit estimate. We do not rule out the possibility of a small primary surplus in 2022.
- In February, interest payments reached BRL26 billion, compared to BRL29.2 billion in February 2021. The result of FX swap operations in the period contributed to this reduction (gain of BRL28.4 billion in February 2022 compared to a loss of BRL5.1 billion in February 2021).
- Debt results were mixed. Gross debt dropped to 79.2% of GDP in February, compared to 79.6% in January. The result was affected by the positive primary surplus in the month and an increase in nominal GDP. Meanwhile, net debt reached 57.1% of GDP, compared to 56.7% of GDP in January.
- Our 2022 gross-debt-to-GDP forecast is currently at 80.6%, virtually stable compared to 2021. We continue to foresee a deterioration in the nominal (headline) budget results due to higher debt costs (in the Selic rate), implying a still steep upward trajectory for government debt in the medium term. Yet, in the short term, this nominal result will be partially offset by the BCB's profit from FX swaps in 2022 (currently above BRL100 billion).

According to BCB data published today, the consolidated public sector posted a primary surplus of BRL3.5 billion in February, better than our forecast (-BRL8.6 billion) and the market's median estimate (-BRL8.3 billion). This was the best result for the month in the historical series. In 12 months, the public sector reached a primary surplus of BRL123.4 billion (1.4% of GDP), compared to BRL64.7 billion (0.75% of GDP) in December 2021.

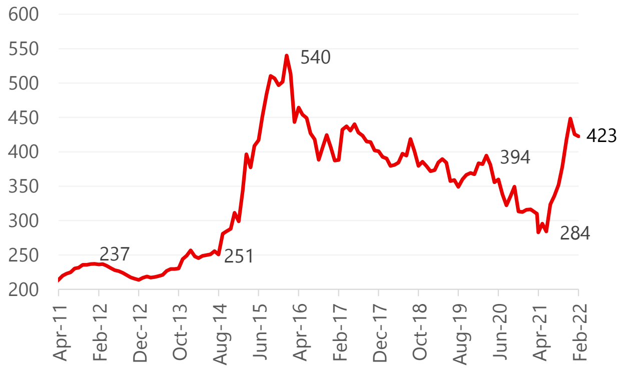
In February, interest payments reached BRL26 billion, compared to BRL29.2 billion in February 2021. The result of FX swap operations in the period contributed to this reduction (gain of BRL28.4 billion in February 2022 compared to a loss of BRL5.1 billion in February 2021). The nominal budget balance reached BRL299.1 billion (3.4% of GDP), compared with BRL383 billion (4.4% of GDP) in December 2021.

Figure 1 – Consolidated Public Sector Result



Sources: Brazilian Central Bank, Santander.

Figure 2 – Nominal Interest Result – BRL billion



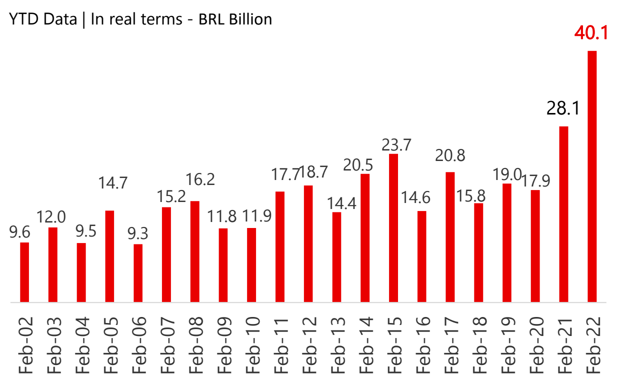
Sources: Brazilian Central Bank, Santander.

In February, regional governments' primary result (BRL20.2 billion) was again the main surprise relative to our fiscal forecast (BRL12.4 billion). In the 12-month reading, regional governments' surplus reached an impressive BRL112.5 billion (1.3% of GDP). In 2021, the subnational entities' primary fiscal surplus was BRL97.7 billion (1.1% of GDP), the all-time high both as a percentage of GDP and in terms of real values in the full year result. In 2020, there was a surplus of BRL38.7 billion (0.5% of GDP) owing to the fiscal stimulus (BRL78.2 billion in direct federal transfers to mitigate the pandemic's effects) and the activity recovery. In 2019, there was a surplus of BRL15.2 billion (0.2% of GDP).

In our view, subnational entities should continue to present positive results in the short term. Our forecast for 2022 is a surplus of BRL45 billion (0.5% of GDP), though this projection is highly dependent on the duration of the price shock effect. February's result adds a positive bias to our estimate.

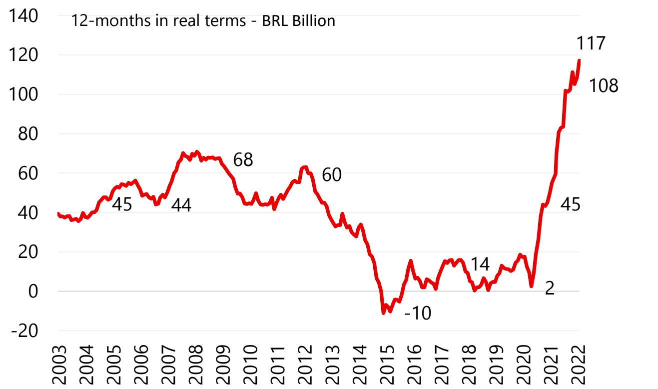
However, in the coming years we believe that regional governments could face the challenge of reestablishing the fiscal balance as fiscal and monetary stimuli come to an end—mainly, in our view, because of pressure to increase mandatory expenditures in the following year (for example, pressure to increase public servants' wages after years without a nominal increase).

Figure 3 – Regional Gov.– Primary Result – YTD Data



Sources: Brazilian Central Bank, Santander.

Figure 4 – Regional Gov. – Primary Result – 12-Month Data



Sources: Brazilian Central Bank, Santander.

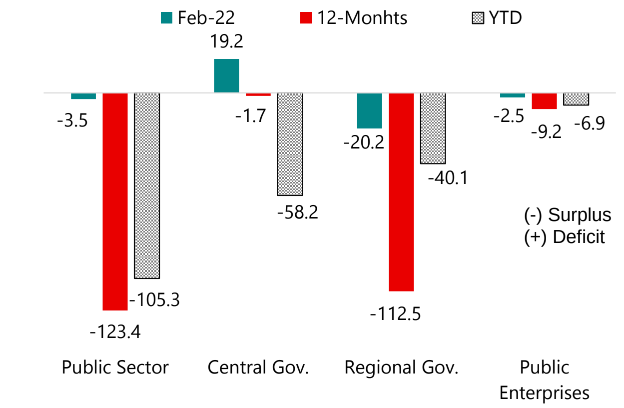
According to data published by the Treasury on March 24, the central government posted a primary deficit of BRL20.6 billion in February. With this result, the 12-month rolling balance continues to run close to zero and is seeing its best performance since October 2014. Expenditures rose 6.5% YoY in real terms, with a higher-than-expected increase in heath expenditures. Revenue rose 14.8% YoY, favored by extraordinary oil-related Transfer of Rights revenue (BRL11.2 billion). For 2022, our forecast points to a central government deficit of BRL45 billion (0.5% of GDP), based on an increase in expenditures and some softening in revenue growth. However, we see risks skewed to the upside because of commodity-driven revenue.

In light of this, adding central and regional government estimates for this year, we forecast a balanced public sector result in 2022, considering an increase in expenditures and some softening in revenue growth—although a more lasting price shock effect on revenue could add a positive bias for the deficit estimate.

Regarding debt statistics, gross debt dropped to 79.2% of GDP in February, compared to 79.6% in the previous month. The result was affected by the positive primary surplus in the month and an increase in nominal GDP. Meanwhile, net debt reached 57.1% of GDP, compared to 56.7% of GDP in January.

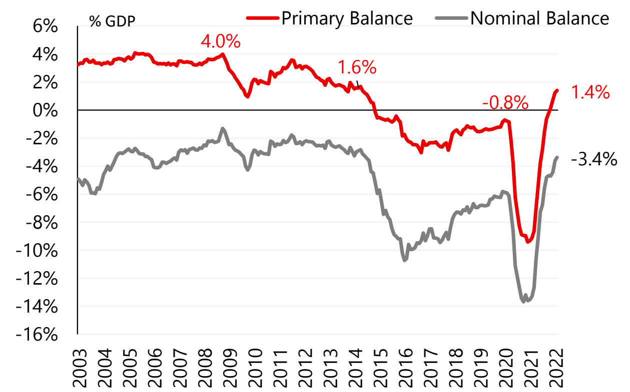
Our 2022 gross-debt to GDP forecast is currently at 80.6%, virtually stable compared to 2021. We continue to foresee a deterioration in the nominal (headline) budget results due to higher debt costs (owing to the Selic rate), implying a still steep upward trajectory for government debt in the medium term. Yet, in the short term, this nominal result will be partially offset by the BCB's profit from FX swaps in 2022 (currently above BRL100 billion).

Figure 5 – Primary Result (BRL billion)



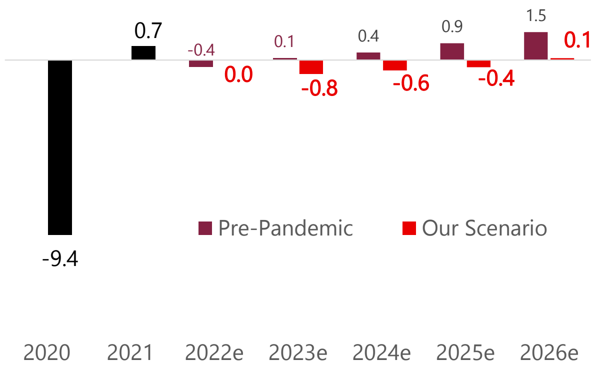
Sources: Brazilian Central Bank, Santander.

Figure 6 – Consolidated Public Sector (12m % GDP)



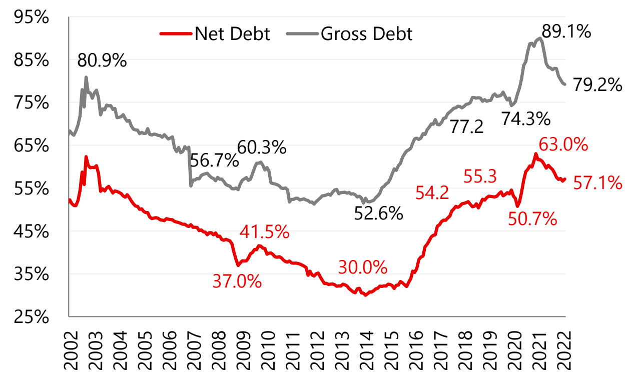
Sources: Brazilian Central Bank, Santander.

Figure 7 – Primary Result Forecast (% GDP)



Sources: Brazilian Central Bank, Santander.

Figure 8 – Public Sector Debt (12m % GDP)



Sources: Brazilian Central Bank, Santander.

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