

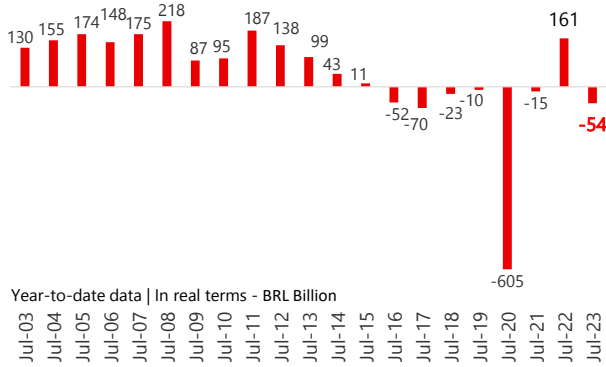
## **PUBLIC SECTOR: JULY'S PRIMARY DEFICIT DEEPENS IN 12 MONTHS**

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- Today, the Brazil Central Bank (BCB) released the consolidated public sector's fiscal balance for July. The public sector posted a primary deficit of BRL35.8 billion, above our forecast (BRL32.2 billion) and the market median estimate (BRL30.2 billion). Regional governments' result accounts for the main difference from our forecast, with a BRL4.2 billion primary deficit compared to our expectation of +BRL3 billion. Subnational entities fiscal balance has shown higher than usual volatility each month this year. We observed a 0.3% YoY rise in states' revenues in nominal terms. Overall, we continue to see the public sector's fiscal performance gradually deteriorating.
- In the 12-month reading, the public sector's primary deficit fell deeper into the negative territory, reaching a primary deficit of BRL80.5 billion (0.8% of GDP) in July, vs. -BRL24.2 billion (0.4% of GDP) in June, and after peaking at 2.4% of GDP (surplus) in July 2022. Regional governments reached a surplus of BRL13.7 billion (0.1% of GDP), vs. the peak registered in May 2022 (BRL128.7 billion, or 1.4% of GDP). Despite the solid recent performance, we believe that fiscal expansion already in the pipeline (~2.0 p.p. of GDP), in the context of softening commodity prices and real activity, will drive the primary deficit to BRL100 billion, or 1.0% of GDP, by the end of 2023. The result will be closely related to the performance of commodity prices, in our view. We are also seeing a limited impact from the measures already implemented by the administration to address the deficit, and it will be important to monitor tax collection in the coming months.
- According to August 30 Treasury data, the central government posted a primary deficit of BRL35.9 billion in July, above our call (-BRL32.1 billion). In the 12-month reading, the primary deficit increased to BRL97 billion (0.95% of GDP), from a deficit of BRL41.5 billion (-0.4% of GDP) in June and a primary surplus of BRL18.2 billion (0.2% of GDP) in May. This happened on the heels of an expected increase in expenditures, especially those related to fiscal benefits. In addition, we have observed a cyclical drop in tax collection and a weak performance of some measures adopted by the government to reduce the tax breaks. In YTD terms, net revenue continued to lose steam (-5.3% YoY real) and expenditures rose (+31.1% YoY real). The latter was due to the impact of the Pension Benefit Bonus (13th payment) calendar change. Normalizing the Pension Benefits, the rise would be ~16% YoY, with higher payments of the wage bonus ("*Abono Salarial*"). For 2023, we forecast a BRL115 billion primary deficit (-1.1% of GDP).
- Interest payments totaled BRL46 billion in July, compared to BRL43 billion in July 2022. In the 12-month reading, the nominal deficit totaled BRL722 billion (7% of GDP), +0.54 p.p. compared to the June 2023 result and up from the BRL460 billion (4.6% of GDP) reported in December 2022. We believe that interest payments will end the year slightly above 8% of GDP.
- In July, debt rose compared to June. Gross debt increased to 74.1% of GDP (+0.5 p.p.). Net debt went up to 59.6% of GDP (+0.6 p.p. in the month), on the heels of interest accrual (+0.4 p.p.) and the primary deficit result (+0.3 p.p.). Voluntary deposits into the Central Bank (not included in debt statistics) declined slightly, to 0.9% of GDP (-0.2 p.p.). Our 2023 gross-debt-to-GDP forecast is currently at 77%, considering a reduction in the nominal GDP deflator tracking based on lower wholesale inflation (IGPs).

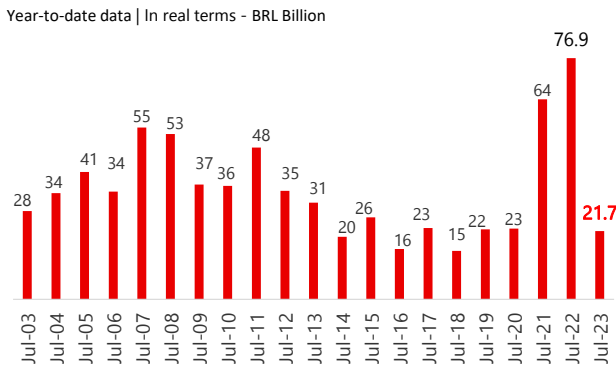


**Figure 1 – Consolidated Public Sector Result**



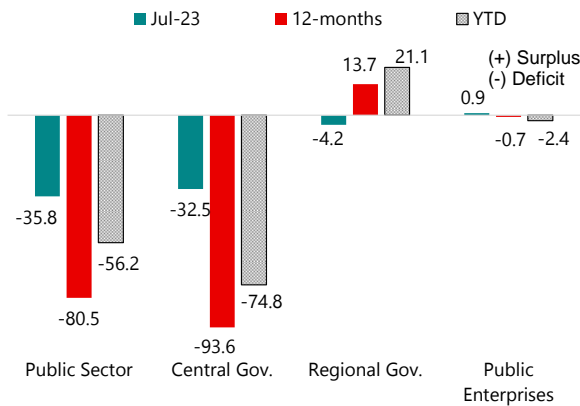
Sources: Brazilian Central Bank, Santander.

**Figure 3 – Regional Gov.– Primary Result**



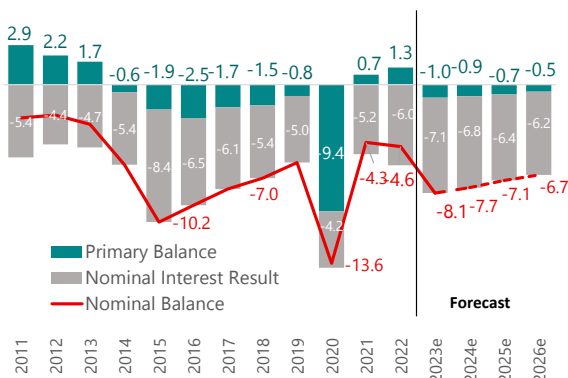
Sources: Brazilian Central Bank, Santander.

**Figure 5 – Primary Result (BRL billion)**



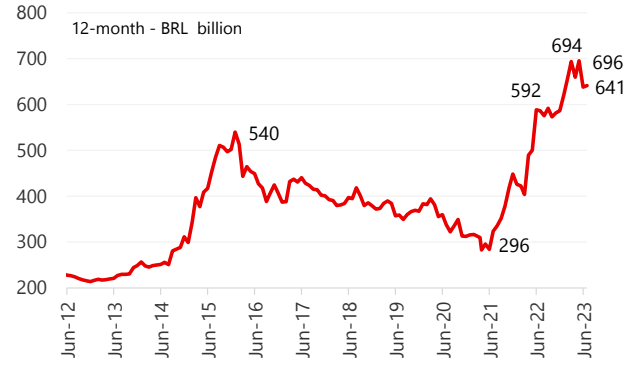
Sources: Brazilian Central Bank, Santander.

**Figure 7 – Fiscal Balance (% GDP)**



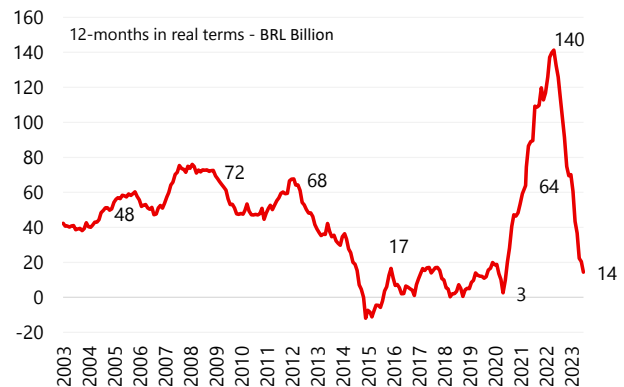
Sources: Brazilian Central Bank, Santander.

**Figure 2 – Nominal Interest Result – BRL billion**



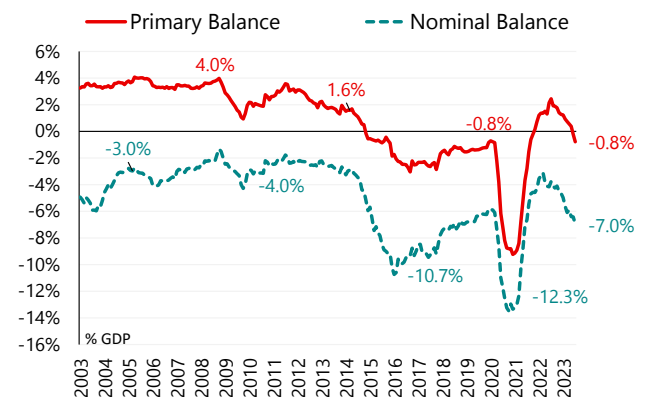
Sources: Brazilian Central Bank, Santander.

**Figure 4 – Regional Gov. – Primary Result – 12-m**



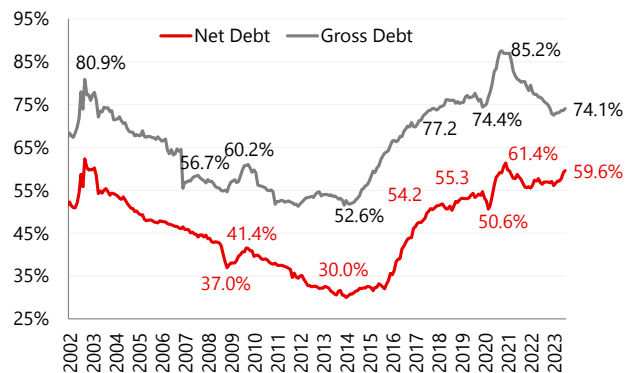
Sources: Brazilian Central Bank, Santander.

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



Sources: Brazilian Central Bank, Santander.

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



Sources: Brazilian Central Bank, Santander.



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