



Brazil Macro | October 2021

FISCAL POLICY

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Summary - Pre-Pandemic Levels with a Bumpy Road Ahead

- The government announced a new welfare program with the monthly stipend upped to BRL 400 for 17 million families. The PEC of *Precatórios* (a constitutional amendment) will likely create the legal vehicle for the new welfare program. The new legislation could further weaken the role of the constitutional spending cap as a fiscal anchor.
- We continue to upgrade our fiscal estimates for 2021, considering higher revenue, boosted by the inflation-effect and commodities boom. We recently added the new one-off revenues (BRL15 billion) for regional government result. Our primary deficit estimate is 0.5% of GDP, yet with a positive bias. Considering the current version of PEC dos *Precatórios* the federal government expenditures could rise by 0.1-0.2 pp of GDP, with new Covid-19 outlays.
- For 2022, we forecast a higher deficit (1.3% of GDP), with a rise in court-ordered debt and other expenses disbursements. We assume an execution of BRL30 billion outside the spending cap, which will likely affect the primary result depending on the final legislation. In PEC of *Precatórios*, the change in indexation of the spending cap rule could add BRL50 billion more to the primary result, increasing the deficit forecast by 0.3-0.4 p.p.
- For the gross debt, we continue to forecast an upward trajectory for the medium term, with the path to a long-term stabilization looking increasingly riskier. Additionally, the fiscal risks remain in the spotlight, with the discussion of the 2022 budget proposal and fiscal legislation debates.

Brief Overview

01

Fiscal – An Overview

Short-run improvement

⇒ Primary Balance: better 2021 result

1.1 Central Government (Deficit BRL25 bn lower)

- More revenues from Oil production and Inflation (Royalties revenues BRL90 bn in 2021: +BRL8 bn)
Terms of trade impact maintained at +0.3pp of GDP)
- Rise in "unused" budget resources to BRL20 bn
- PEC of *Precatórios* could rise "extra-cap" outlays in +BRL15 billion

1.2 Regional Gov. all-time record

- Surplus in 2021 to BRL65 bn (from BRL40 bn)
(In the tracking this could reach a level above BRL80bn)

⇒ Gross Debt close to 80% of GDP

(3/4 of the reduction due to price shock)
The cost is still contained (yet it is increasing)

⇒ Debt Liquidity Reserves Level

(Reaching more than BRL1 trillion, covers close to 11 months of debt maturities)



Risks: A Bumpy Road Ahead

⇒ Binding Spending Cap Margin

(PEC of *Precatórios* could change the index and increase the margin in BRL60 billion for 2022. This means a shift in the fiscal rule)

⇒ Congressional Debate -

1. Court-ordered debts Conundrum

(Sub-cap BRL40bn paid under the spending cap)

2. "Auxílio Brasil" New Welfare Program

(BRL82 bn budget – 17mi families BRL400/mo)

3 Pressure for more expenditures

(Auxílio-gas, Payroll Tax Breaks, Emergency Aid, payback of Expenditures post-Covid19)

⇒ Fiscal Outlook - Riskier

1. Primary Balance in 2024-25

(Depend on Inflation Scenario and the fiscal framework debate, We included more court-ordered debt payments)

2. Gross Debt Trajectory

(94% of GDP, rise in debt costs, +2.0 pp of GDP)
PEC of *Precatórios* could imply in a +6.0p.p shift

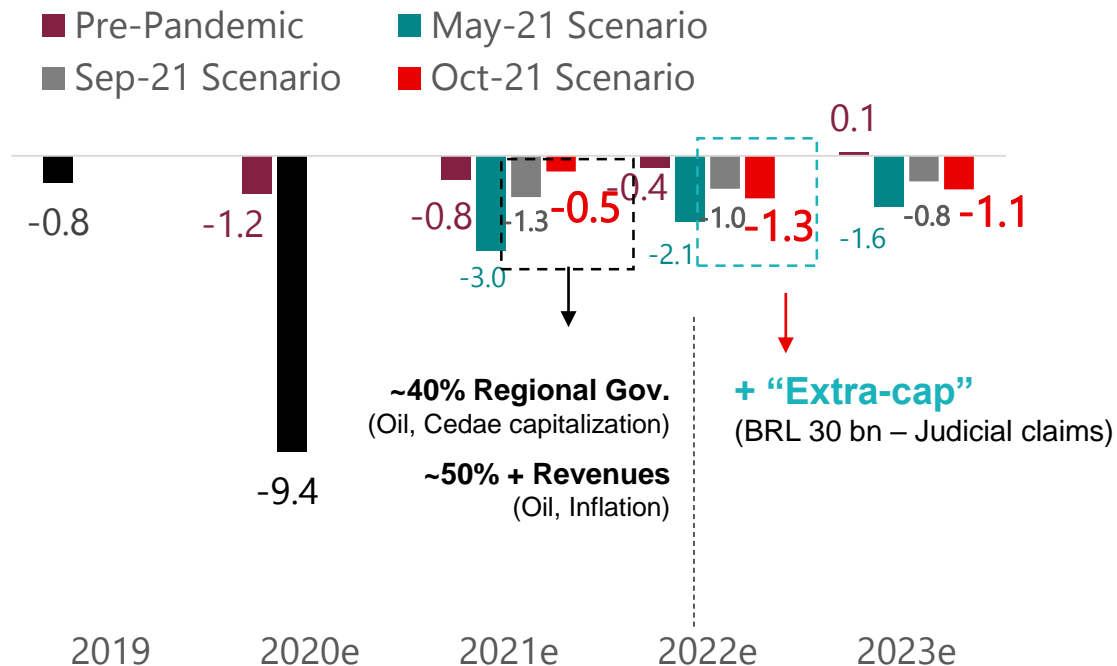
Fiscal Scenario and PEC of *Precatórios* Simulations

02

Fiscal – Revised Trajectory for Primary Balance and Gross Debt

- Considering the terms-of-trade and inflation impact on the revenues we improved our forecasts for the primary result. Yet, a more persistent improvement will depend on the commodity boom.
- The inflation shock's impact directly accounts for 3/4 of the improvement (primary and GDP deflator) in the debt-to-GDP.**

Public Sector Primary Result (% GDP)



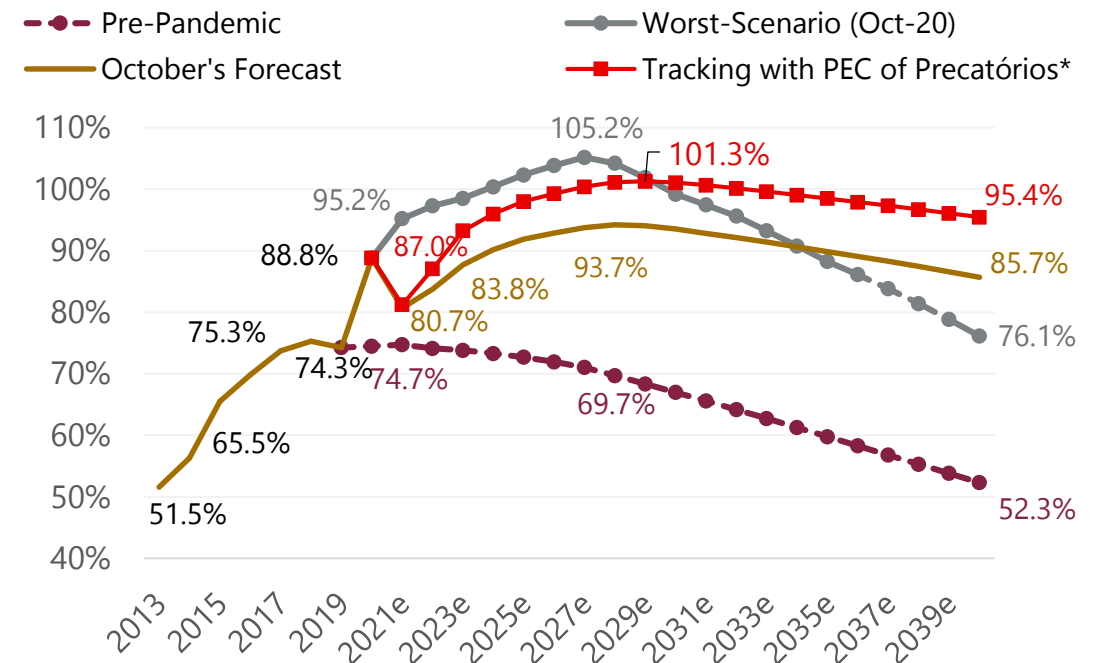
Sources: BCB, Santander.

PEC of *Precatórios* possible effect:

2021: Extra-cap: +BRL15 bn
 2022: +BRL 60 bn in expenditures
 – deficit would go to 1.7% of GDP



Scenarios - Gross Debt Scenario (% GDP)



Sources: BCB, Santander

- PEC of *Precatórios*:** could add more +BRL110 billion in expenditures changing the spending cap rule and compressing the court-ordered debt budget

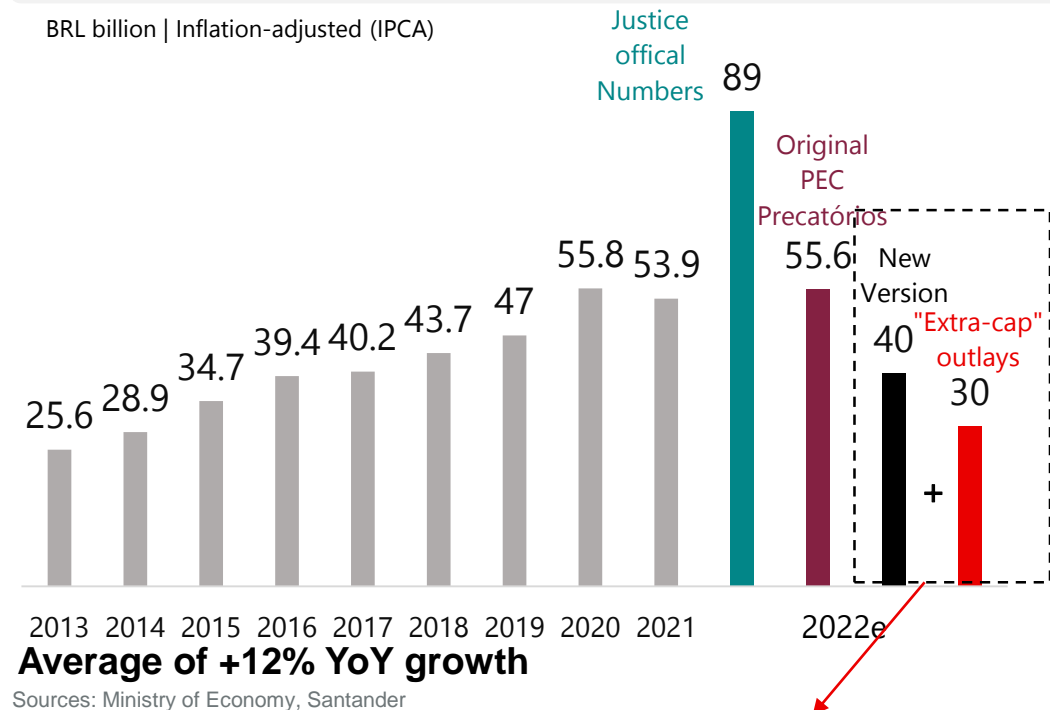
Hypothesis: Deficit: -0.5% in 2021 | -1.7% of GDP in 2022.

Selic rate: 9.25% YE2021 | 11.5% YE2022 | 9.0% YE2023 | 7.0% onwards

Fiscal – PEC Precatórios will likely create the legal vehicle for the new welfare program

- The government announced its intention to increase the new welfare program monthly benefit to a minimum of BRL 400 for 17 million families. The source of funding for the program is still unclear, especially for 2022. To achieve this goal, the government could approve the constitutional amendment (PEC Precatórios) to “solve” the court-ordered debt conundrum by limiting this expenditure to BRL40 billion for 2022 (out of BRL89 billion) to open a fiscal margin of BRL50 billion, removing this value from the spending cap limit. In addition, the new version of the PEC, approved on October 21 in the Lower House Special Commission, included a change the index used to readjust the spending cap rule since 2016 (changing the year-on-year IPCA inflation window from June to December).

Judicial Claims Increase – BRL billion



- * **BRL 70 bn total payments**
 - BRL40 bn limited to the spending cap rule
 - BRL30 bn “extra-cap” outlays
- * **BRL19 bn: offsetting state debts + discounts**

2022 Spending Cap Margin - Simulation

2022 Budget: Spending Cap Margin - BRL bn						
Court-ordered debts Budget ("Precatórios")						
BRL bn		40	50	75	89	90
Year-end Inflation (INPC Dec-21)	7.0%	49	39	14	0	-1
	7.5%	44	34	9	-5	-6
	8.0%	40	30	5	-9	-10
	9.5%	25	15	-10	-24	-25
	10.0%	22	12	-14	-28	-29
	10.5%	24	14	-20	-25	-26
Additional Budget for Auxílio Brasil- BRL bn						
Monthly Average Benefit (BRL/month)						
		300	350	400	500	600
Families (millions)	17	26	36	47	67	87
	16	23	32	42	61	80

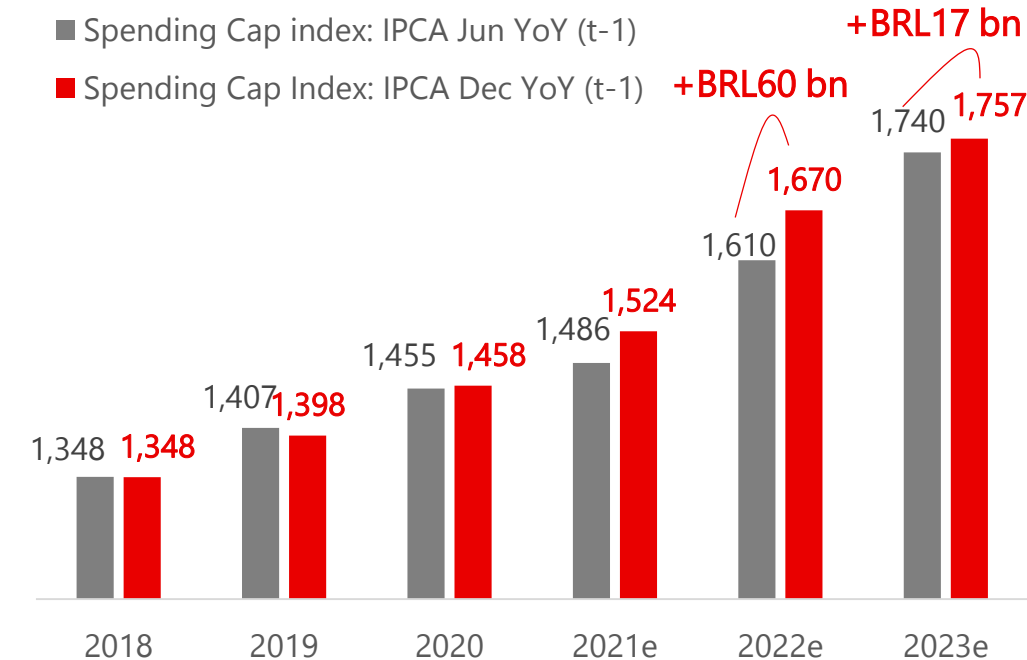
Bolsa Família's current budget (2021): BRL35 billion/year | Total: 14.6 million families

Sources: Santander

Fiscal – *PEC of Precatórios* will likely create the legal vehicle for the new welfare program

- *PEC Precatórios* current proposal would create an addition space of about BRL110 in the spending cap rule (BRL50 bn through court-ordered debt cap + BRL60 bn by changing the spending cap indexation rule)
- In this scenario, the fiscal margin for 2023 will be BRL17 billion higher, using our inflation forecasts.

Change in the index of Spending Cap Rule



○ IPCA 12m Jun: 2021: 2.1% | 2022: 8.4% | 2023: 8.1%

○ IPCA 12m Dec: 2021: 4.5% | 2022: 9.6% | 2023: 5.2%

Change in the index of Spending Cap Rule

Simulation changing the spending cap index since 2016 to IPCA 12m **December** (t-1) from IPCA 12m **June** (t-1)

Yearly difference between the indexes above*:

2018: -0.1%

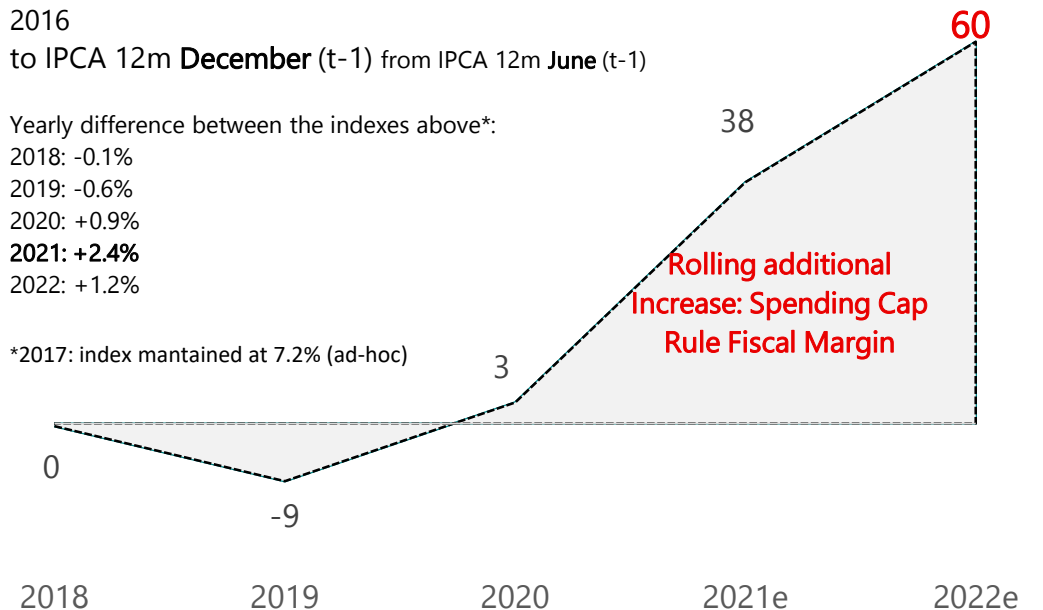
2019: -0.6%

2020: +0.9%

2021: +2.4%

2022: +1.2%

*2017: index maintained at 7.2% (ad-hoc)



Sources: Ministry of Economy, IBGE, Santander

Fiscal – Complex solution to increase the 2022 outlays - SIMULATION

- The government announced a new welfare program with the monthly stipend upped to BRL 400 for 17 million families. The PEC of *Precatórios* (a constitutional amendment) will likely create the legal vehicle for the new welfare program. The new legislation could further weaken the role of the constitutional spending cap as a fiscal anchor.

Santander - Public Finances Tracking		
	BRL Billion	% GDP
2021		
I. Oct-21 Public Sector Primary Deficit Estimate	45	0.5%
II. Additional "Extra-cap" outlays (PEC <i>Precatórios</i>)	15	0.2%
New total "extra-cap" budget	150	1.7%
Our estimate of final "extra-cap" execution	125	1.4%
III. Regional Gov. Surplus increase (currently est. BRL65 bn)	20	0.2%
IV. Higher Revenues from Oil Sector (Dividends + Royalties)	10	0.1%
Tracking Primary Deficit Estimate (I - II + III + IV)	30	0.3%

Sources: Ministry of Economy, National Congress, Santander

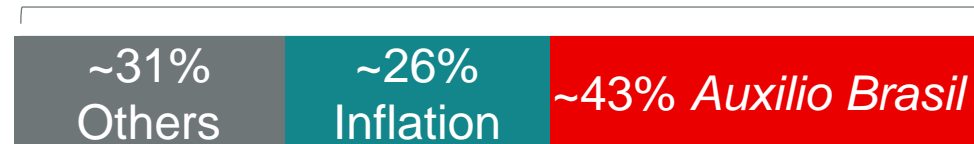
* Considering the approval of PEC of *Precatórios*

Simulation - PEC of *Precatórios* impact in 2022

2022		
Spending Cap Margin Changes:	BRL Billion	% GDP
Current Fiscal Margin (Inflation INPC Dec-21: 10%)	-28	-0.3%
PEC <i>Precatórios</i> Changes		
Capping Court-Ordered Payments to BRL40 bn (our of BRL89 bn)	50	0.5%
Changing the Fiscal Rule Indexation (by changing the YoY IPCA window from Jun to Dec)	60	0.6%
New Fiscal Margin (post PEC <i>Precatórios</i>)	110	1.3%
New Expenditures for the new margin		
Increase in Mandatory Outlays (Higher Inflation)	-28	-0.3%
New welfare program expansion (Total Budget BRL82 bn)	-47	-0.5%
750k Truckers Drivers BRL400 benefit	-4	0.0%
Others expenses- 2022 budget	-31	-0.3%
Total New Expenitures	-110	-1.2%
Primary Deficit Estimate (Preliminary)	155	1.7%

Sources: Ministry of Economy, National Congress, Santander

BRL110 billion



See the expenditures
in debate in next slide



PEC of Precatórios: the BRL31 billion in the “Others”. What will be debated?

Possible Additional Expenditures (Risks)	
Measure	BRL billion
Budget Rapporteur Amendments	16-20
Electoral Fund	2
Keeping the payroll tax exemption for 2022 (PL 2541/2021) 17 sectors, 6 million Jobs	8.4
Cultural Sector Aid – “Paulo Gustavo Law” (PL 73/2021)	3.9
Benefits for Agricultural Families (PL 823/21) – Overturn the Presidential veto	10.0
“Vale-Gas” (benefit to buy cooking gas)	6
Public Servants wage increase +5.0%	15

Sources: Minister of Economy, Santander

Fiscal Outlook and Risks for 2022 onwards

Compliance to Fiscal Responsibility Law:

The government wants to use the Dividends taxation as the permanent source to finance the new welfare program.

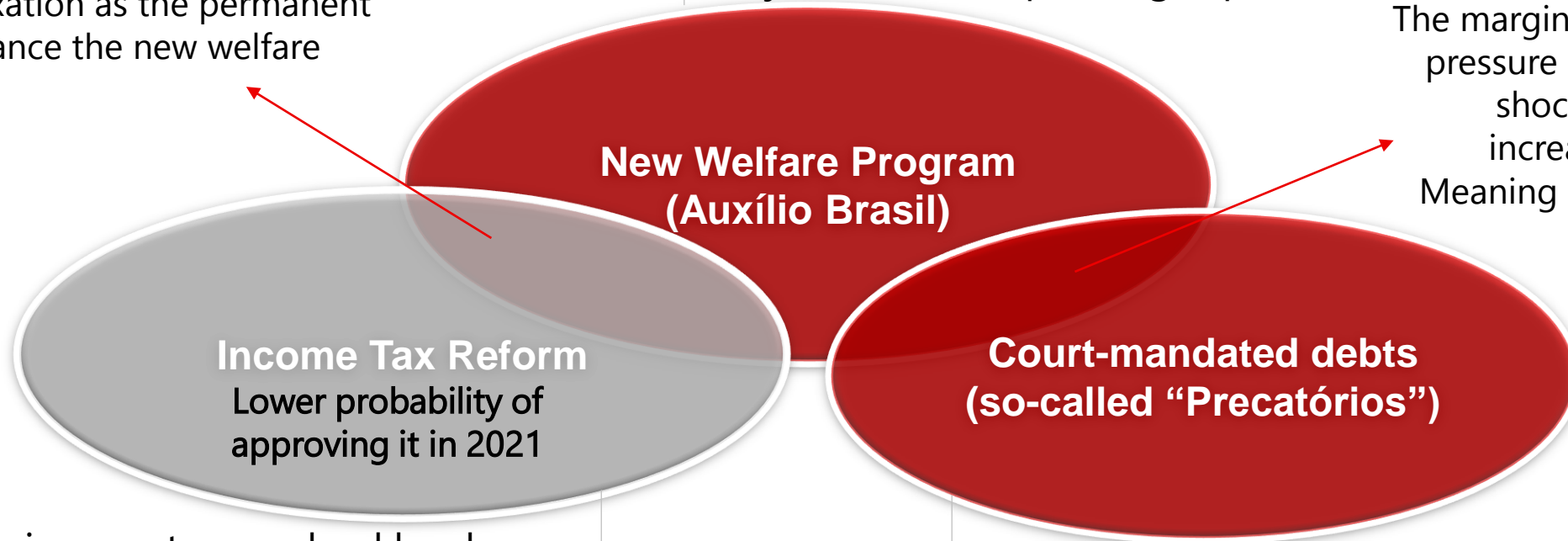
Social Demand to expand the permanent fiscal transfers

Replace the *Bolsa Família* program

Subjected to the Spending cap Limit

Spending cap

The margin for 2022 is under pressure of the inflationary shock in 2H21 and the increase in *Precatórios*. Meaning a limitation to the program's budget



**New Welfare Program
(Auxílio Brasil)**

Income Tax Reform
Lower probability of
approving it in 2021

**Court-mandated debts
(so-called "Precatórios")**

An income tax overhaul has been a government plan since the last presidential run.

Official estimates pointing to a jump in this spending line to ~BRL 90 billion for 2022, beating by and large the government's initial expectation (~BRL 56 billion).

Pressure to the spending cap limit

And If the Income Tax Overhaul Is Not Approved?

How can *Auxílio Brasil* be implemented?

2021

1. Can start in November (at least partially)
2. The Provisional Measure allows the program to start
3. Could increase to 17 million families

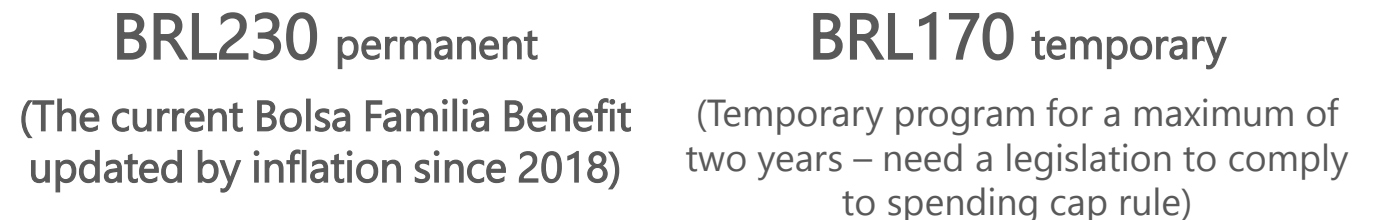
Source of Finance:

Increase in credit IOF (BRL2.1 bn) +
Bolsa Familia savings from beneficiaries
migration to Emergency Aid: BRL9.3 bn

2022 may not have a source of finance to
comply to the Fiscal Responsibility Law

Alternative

BRL400 monthly benefit



Reaching **17 mi** families

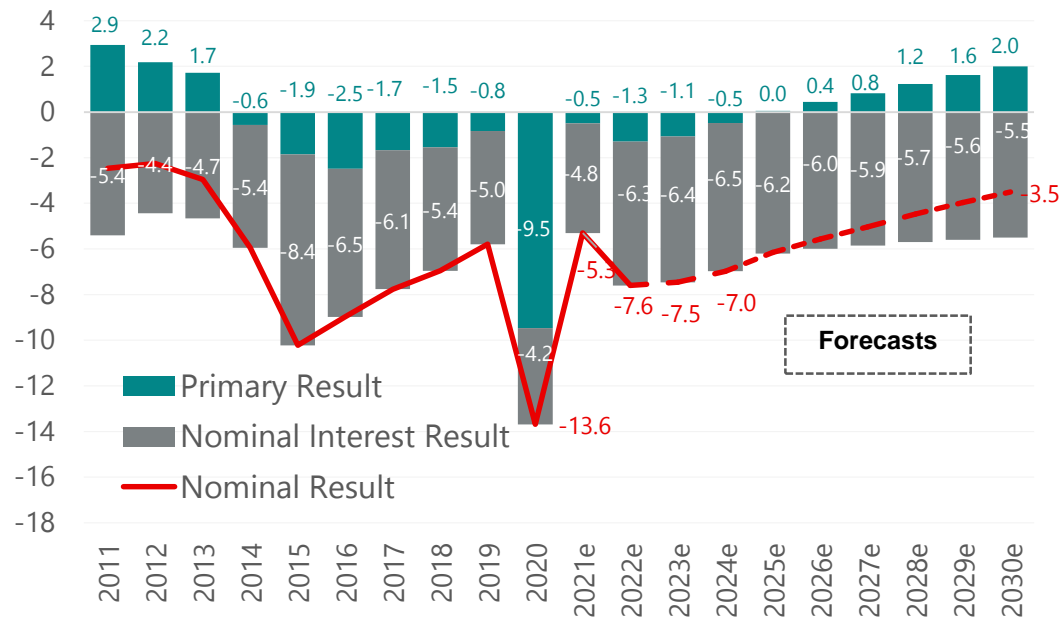
Total Budget: BRL82 bn

(BRL35 bn from Bolsa Família Program + BRL47 bn to complement)

Fiscal – Effects of Higher Selic Rate on Interest Bill and Nominal Deficit

- We revised our nominal Selic rate to 11.5% (tracking) in 2022 (from 9.0% in Oct). The neutral interest rate is at 4.0% per year.
- This will contribute to increase the nominal deficit, specially after 2023.
- The increase in the Selic rate is increasing the Debt during a year, with higher interest accrual. The debt cost will increase to BRL370 billion a year, with the Selic rate at 11%.

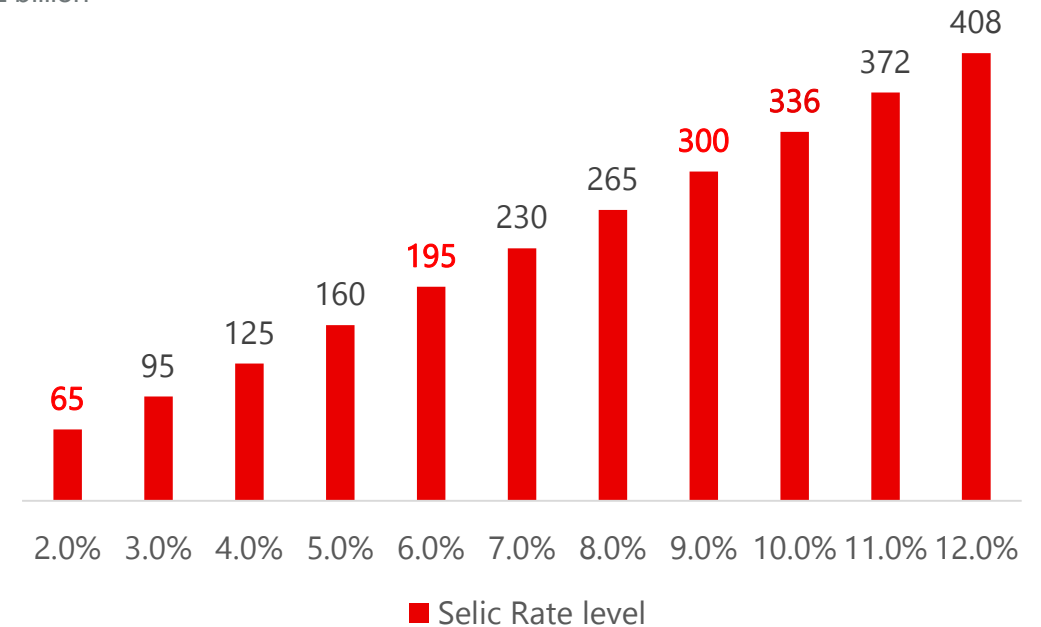
Public Sector's Financing Needs (% GDP)



Sources: BCB and Santander.

Interest Accrual vs Selic Rate Level

BRL billion



Sources National Treasury, BCB and Santander.

PEC of *Precatórios* could change the Nominal Balance Forecasts

- 2021: to -5.6% of GDP
- 2022: to -8.8% of GDP

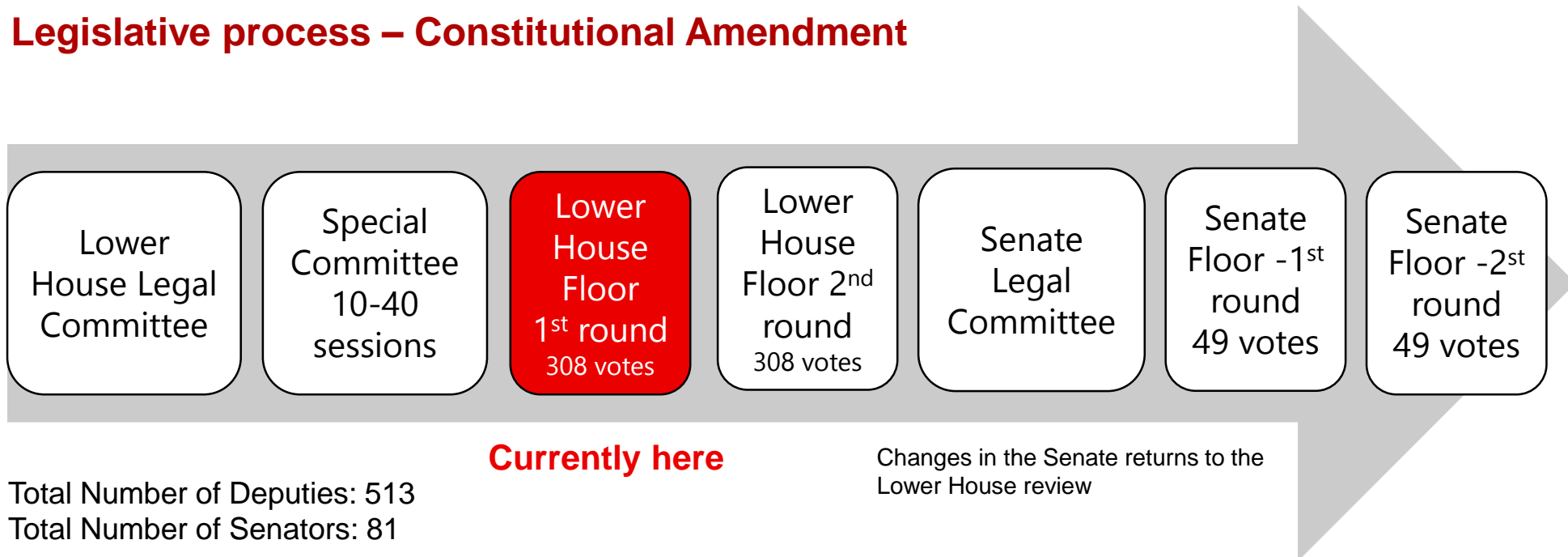
Court-ordered Debt - *Precatórios*

03

Outlook – Legislative Process of PEC *Precatórios*

- The administration unveiled a constitutional amendment (PEC23/2021) proposal to stagger court-mandated debts (so-called “*Precatórios*”), after the official estimate soared to BRL90 billion.

Legislative process – Constitutional Amendment



For the official Gov Presentation of PEC of *Precatórios* (in Portuguese) access at: <https://bit.ly/Gov-PEC-Precatorios>

National Treasury report - The provisions of court-debt orders liabilities

- In a report published on 10/06/2021, it included the provisions for judicial and administrative losses reported by the Attorney General of Brazil, totaling BRL277 billion. These are the official provisions published in the Treasury's "General Budget Report".

Provisions	BRL billion	%
Fundef – ACP	90	32.5
Possessory Action	50	18.1
Indemnity related to readjustment, damages and loss of profits	32.6	11.8
Fundef	30.0	10.8
Fundef actions filed directly by federal entities	17.6	6.4
Prescription of Reimbursement to the Treasury – TCU	7.3	2.6
Fiscal Auditors – 28.9% readjustment	7.1	2.6
Indemnity for material damage	6.4	2.3
Wage Differences	5.3	1.9
Performance Bonus – RAV	4.3	1.5
Others	26.7	9.6
Total	277.0	100

Sources: National Treasury, Ministry of Economy, Santander

Outlook – Judicial Claims official estimate soared, the risks remains high

- The administration unveiled a constitutional amendment proposal to stagger court-mandated debts (so-called “*Precatórios*”), after the official estimate soared to BRL90 billion.

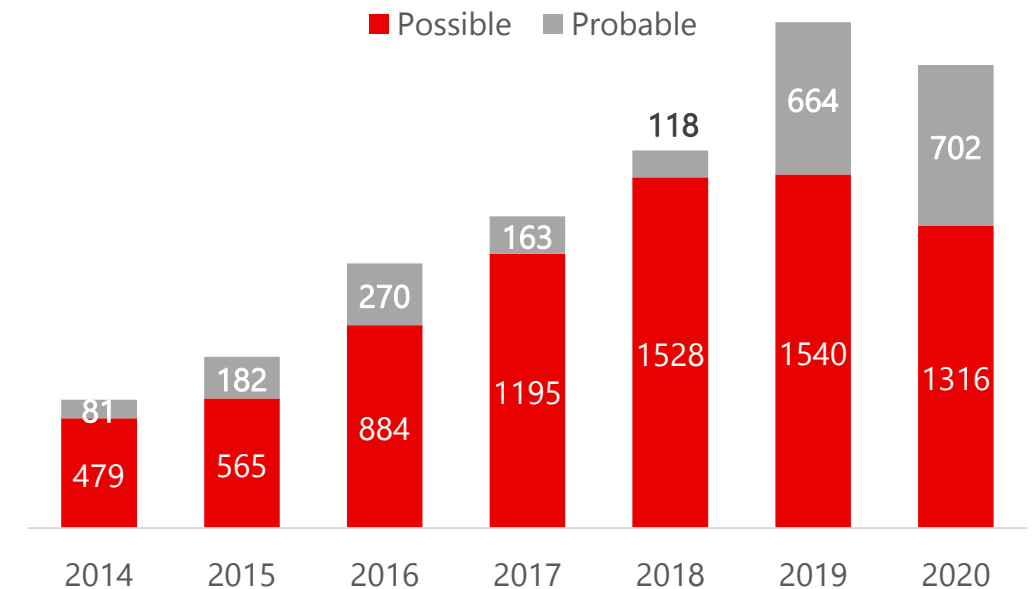
Judicial Claims Increase – BRL billion

BRL Billions	2021	2022
Personnel	10.5	13.7
Judicial Claims	7.3	10.5
RPVs (small value requisitions)	2.1	1.9
Others	1.1	1.3
Pension Benefits	22.6	30
Judicial Claims	10.5	15.7
RPVs (small value requisitions)	12.1	14.3
Continuing Benefits	1.4	1.6
Judicial Claims	0.2	0.3
RPVs (small value requisitions)	1.2	1.4
Other cost capital expenses	20.8	43.7
Judicial Claims	17.7	40.3
RPVs (small value requisitions)	1.9	2.3
Others	1.3	1.1
Total	55.4	89.1

Sources: National Treasury, MCM, Santander

LDO Judicial Claims: Probable and Possible Risk

BRL Billion | Nominal values



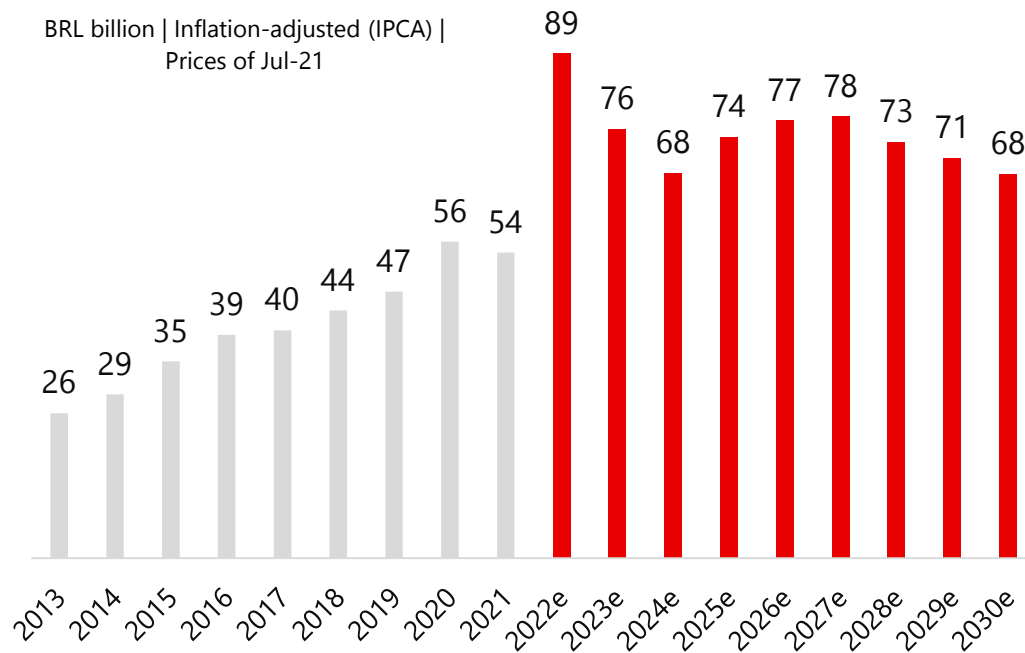
Sources: AGU, LDO 2020, Santander.

This judicial claims are included in the Budget Guidelines (LDO) as a potential and probable fiscal risks. Differently from the previous table from the “General Budget Report”, this numbers are the potential of liabilities in the Supreme Court judgments. 18

We estimate an increase in judicial claims over the next years

- We constructed a forecast based on the LDO probable judicial claim for next the years. In the short-run we see more pressure from the Fundef (BRL90 billion) and those related to pension payments.
- Our preliminary estimate is only a preliminary "educated-guess" in view of the difficulty in estimating and the uncertainties related to the legal process. Either way, it has a relevant fiscal risk and requires a fiscal discipline in management to this increase.

Our Preliminary Estimates for judicial claims budget

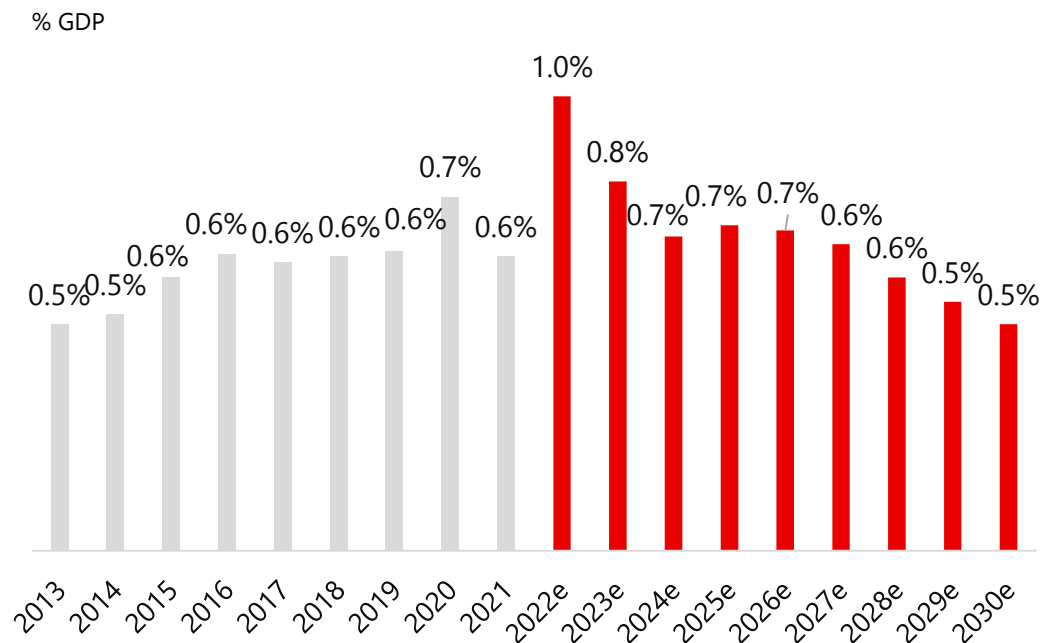


Sources: LDO 2022, Santander

Preliminary Estimates

Based on the LDO 2022 Tables 14 to 20

Judicial claims estimates

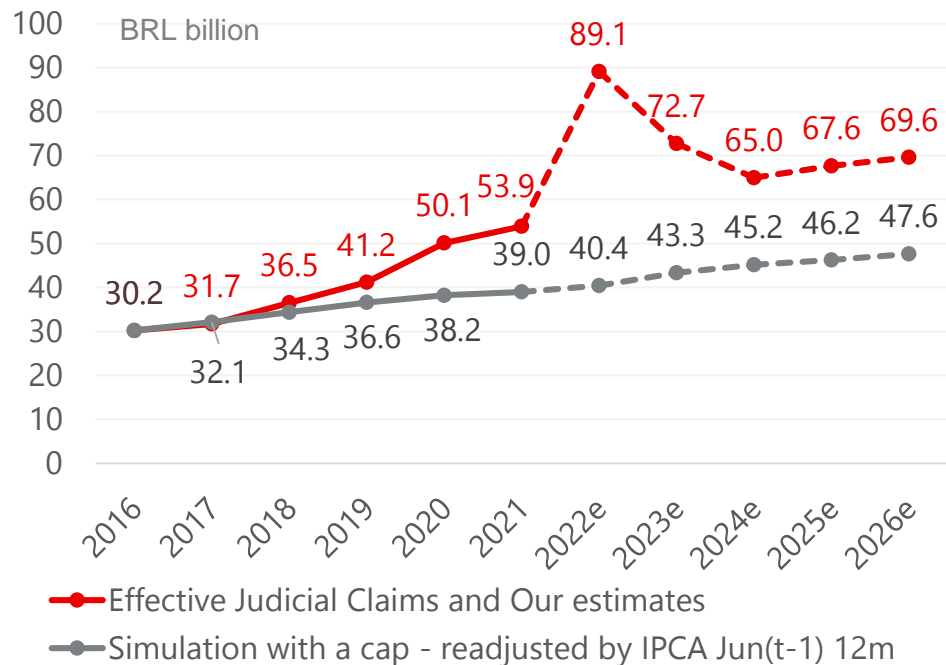


Sources: LDO 2022, Santander

Simulation – possible proposal of creating a cap for the payment

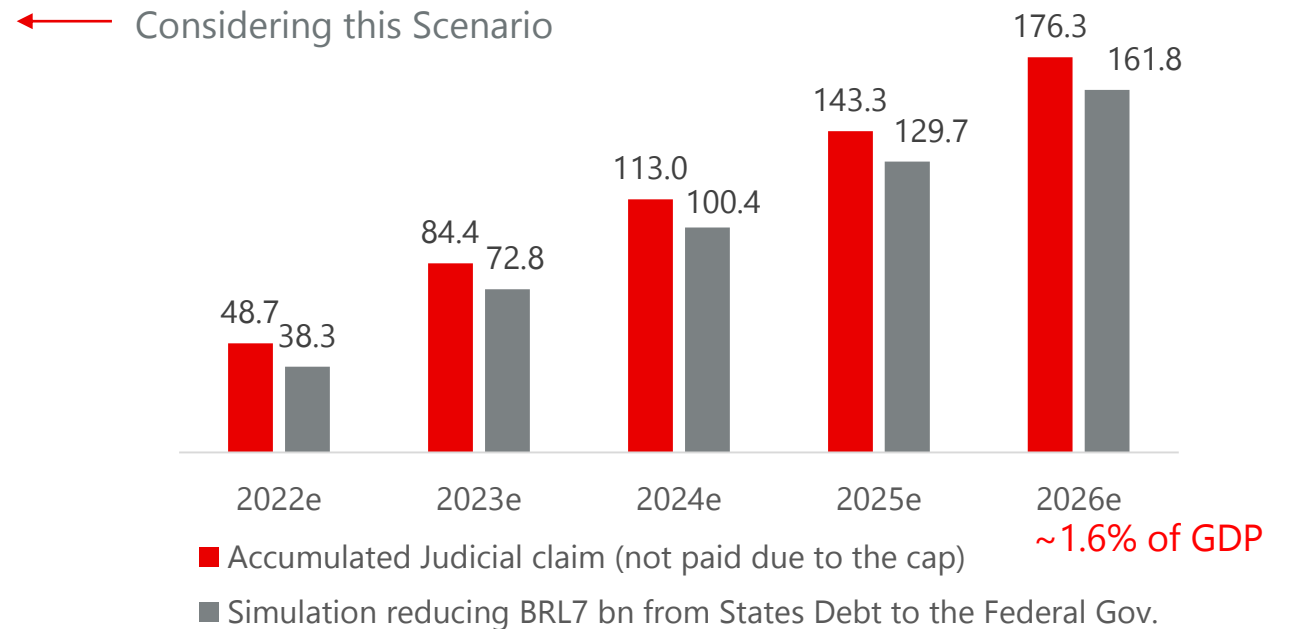
- One of the possibilities discussed to reduce the judicial claims payments would be to create a ceiling for these liabilities and postponing the remaining for the next few years.
- Creating a cap since 2016 would reduce the judicial claim payments in 2022 to close to BRL40 billion, from the BRL89.1 billion official number. We readjusted the judicial claims since 2016 by the Selic rate, yet changing to inflation the results are similar.

Simulation - A limit for Judicial Claims payments



Sources: National Treasury, BCB and Santander.

Simulation with a cap – Accumulated judicial claims



Sources National Treasury, BCB and Santander.

New Welfare Program –
named as *Auxílio Brasil*

04

New welfare program – *Auxílio Brasil*

- Spending cap margin for 2022 is shrinking due to inflation and repressed pension benefits queue. The yearly increase in the judicial claims (reaching BRL89 billion) reduced the fiscal margin under the spending cap limits.

Simulation: New welfare program – BRL billion

Expenses in BRL billion - Yearly Budget							
		Monthly Benefit (BRL)					
		190	300	350	400	500	600
Millions of Families	23	52.4	82.8	96.6	110.4	138.0	165.6
	21	47.9	75.6	88.2	100.8	126.0	151.2
	19	43.3	68.4	79.8	91.2	114.0	136.8
	17	38.8	61.2	71.8	82.0	102.0	122.4
	15	34.2	54.0	63.0	72.0	90.0	108.0
	13	29.6	46.8	54.6	62.4	78.0	93.6
	11	25.1	39.6	46.2	52.8	66.0	79.2

Sources: Santander.

In Green: Current Budget

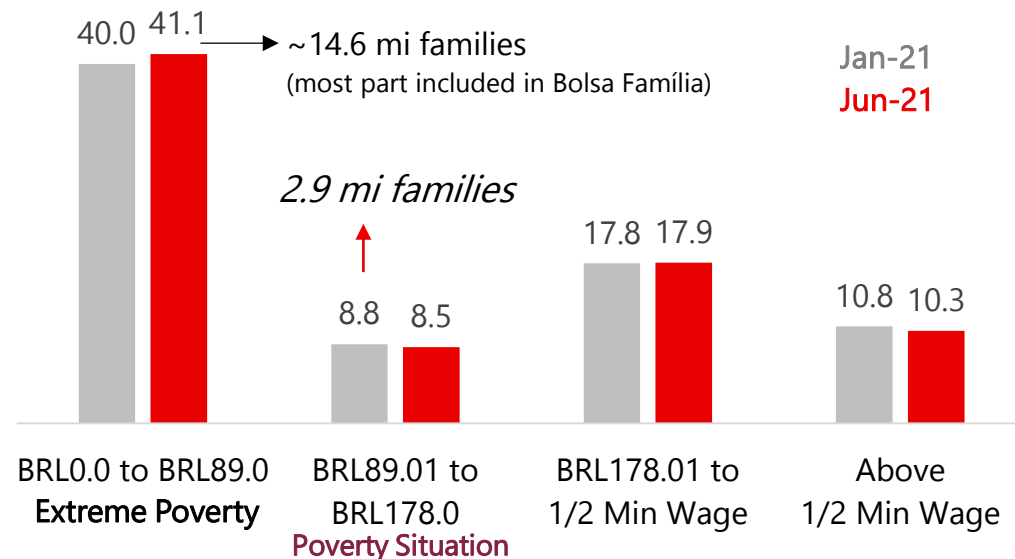
In Red: current values in public debate

New welfare program – *Auxílio Brasil*

- On August 9, the government submitted to congress a provisional measure to create a new welfare program named as *Auxílio Brasil*, in replacement of the Bolsa Família program. The proposed text does not establish the value of the new benefit and, according to the government, the total budget and parameters will be decided in 4Q21.

Cadastro Único – Gov. Database

People Registered in *Cadastro Único* - Monthly Income Per Capita Intervals



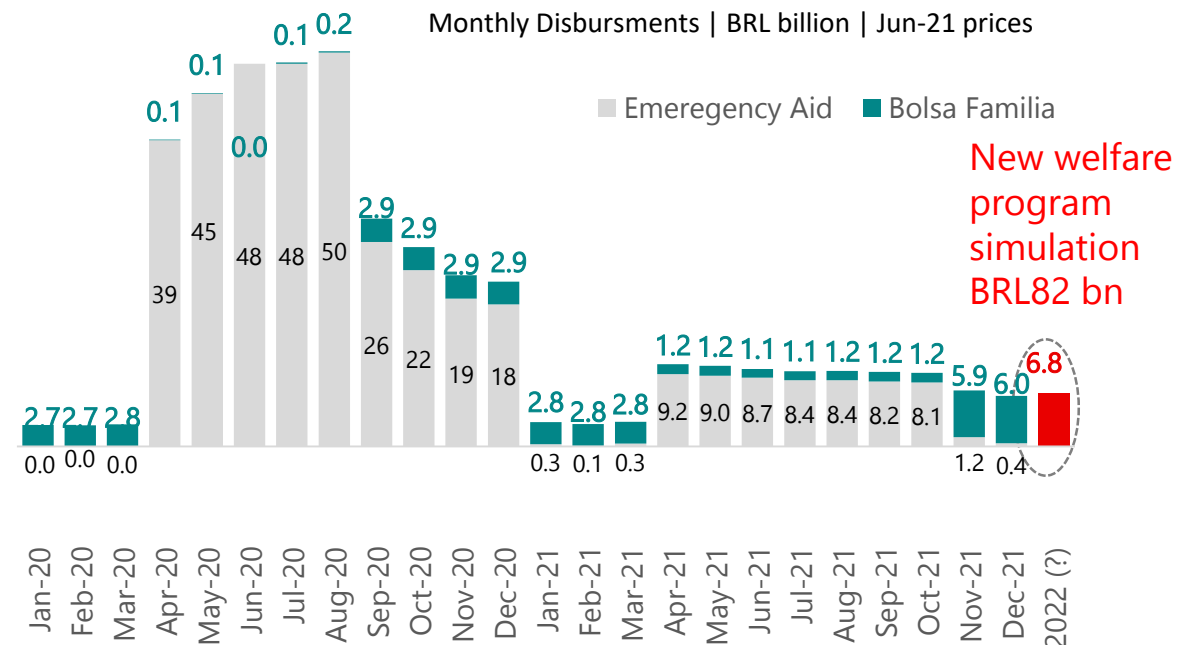
Monthly Income Per Capita

These intervals could be updated in 2022, last time was in 2018.

Sources: Ministerio da Cidadania, Santander



Simulation: New welfare program – BRL billion

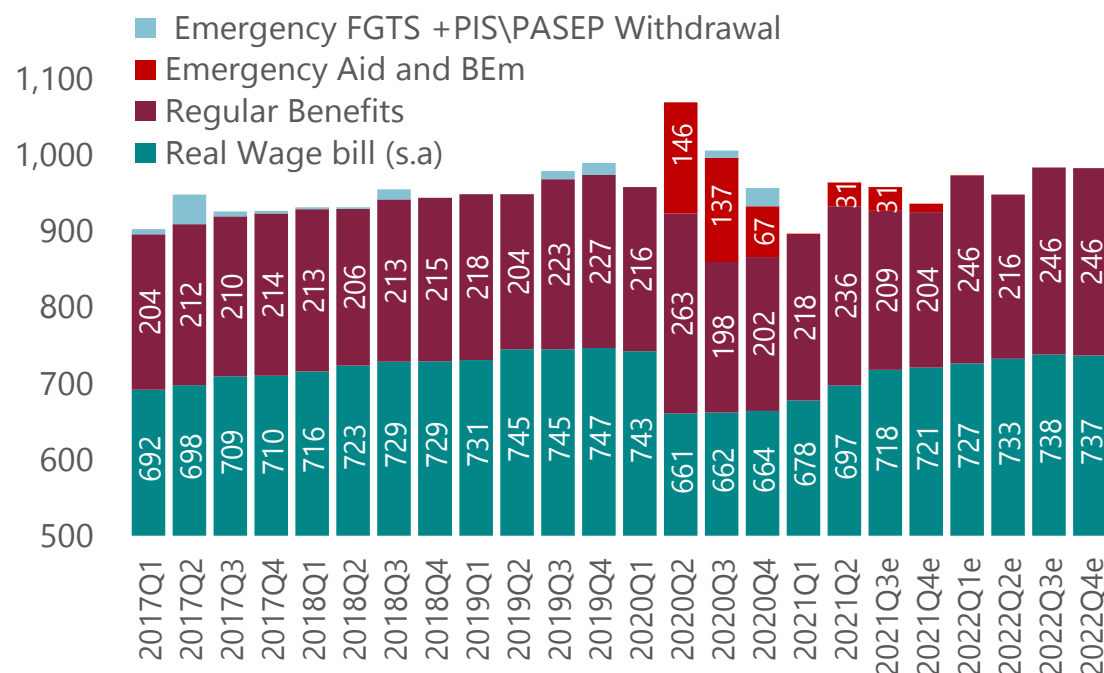


Sources: National Treasury, Santander.

“Expanded” real wage bill will drop in 2021, with partial recovery in 2022

- Considering PEC of *Precatórios*, with the government transfers increase, the overall effect on the real wage bill is neutral. The effect of the new value of the welfare program and the revised value of regular transfers (impact of +1.3p.p.) barely offsets the negative impact of labor income due to inflation and monetary policy (-1.2p.p.). We now expect the “expanded” real wage bill to post 3.5% growth in 2022 (from 3.4% in our last review). Considering the revised levels of inflation and the Selic rate for the alternative simulations, we estimate the growth of the “expanded” real wage bill as between 3.0% and 4.3%. We still consider these scenarios as compatible with an expansion of household consumption of around 1.0% in 2022.

“Expanded” Real Wage Bill (BRL billion)



Sources: National Treasury, IBGE, Ministry of Economy, Santander.

	2020	2021(E)	2022(E) - Selic Rate Simulation		
			10.00%	11.50%	13.00%
Real Wage Bill (No Fiscal Stimulus)	-7.9%	+3.3%	+4.6%	+4.2%	+3.7%
Real Wage Bill (Fiscal Stimulus + Auxílio Brasil BRL35bn)	+3.7%	-5.8%	+2.7%	+2.4%	+2.1%
Real Wage Bill (Fiscal Stimulus + Auxílio Brasil BRL82bn)			+3.9%	+3.5%	+3.2%

Sources: National Treasury, IBGE, Ministry of Economy, Santander.

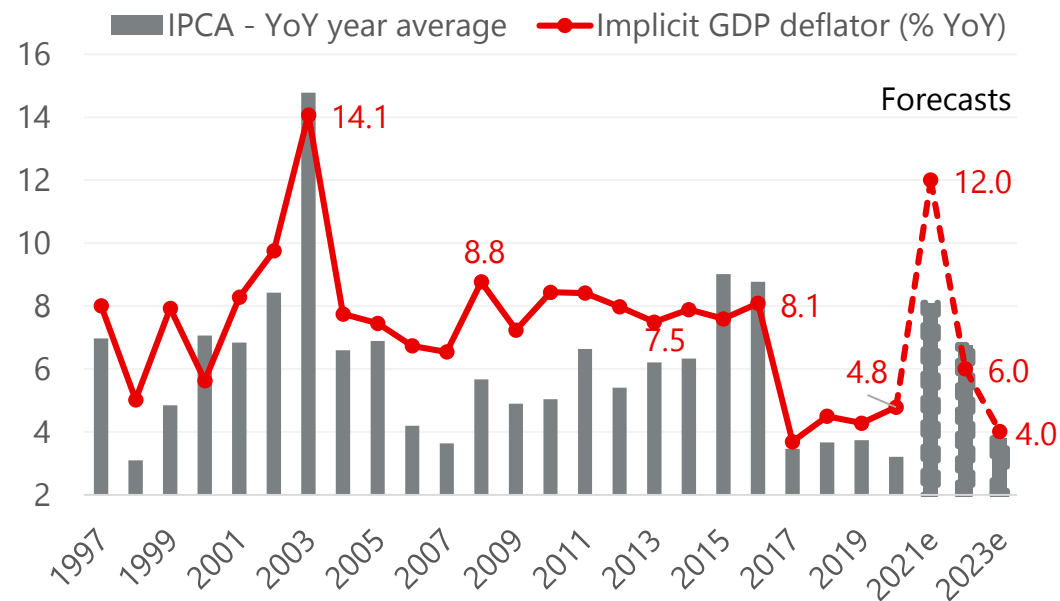
Fiscal background – Price
shock impact

05

GDP Deflator Impact – Terms-of-Trade and Inflation Shock Effect

- One of the main effects of both higher inflation and activity recovery is higher nominal GDP, which consequently affects the debt-to-GDP ratio. At the beginning of the year, we estimated that nominal GDP would increase by 7% in 2021; our latest tracking points to a ~18% increase. The main effect was on the GDP deflator, which went from 4.0% to 12%, closely related to the commodity shock and an increase in the IPCA forecast from 3.6% (February) to 9.6% (in our latest tracking).

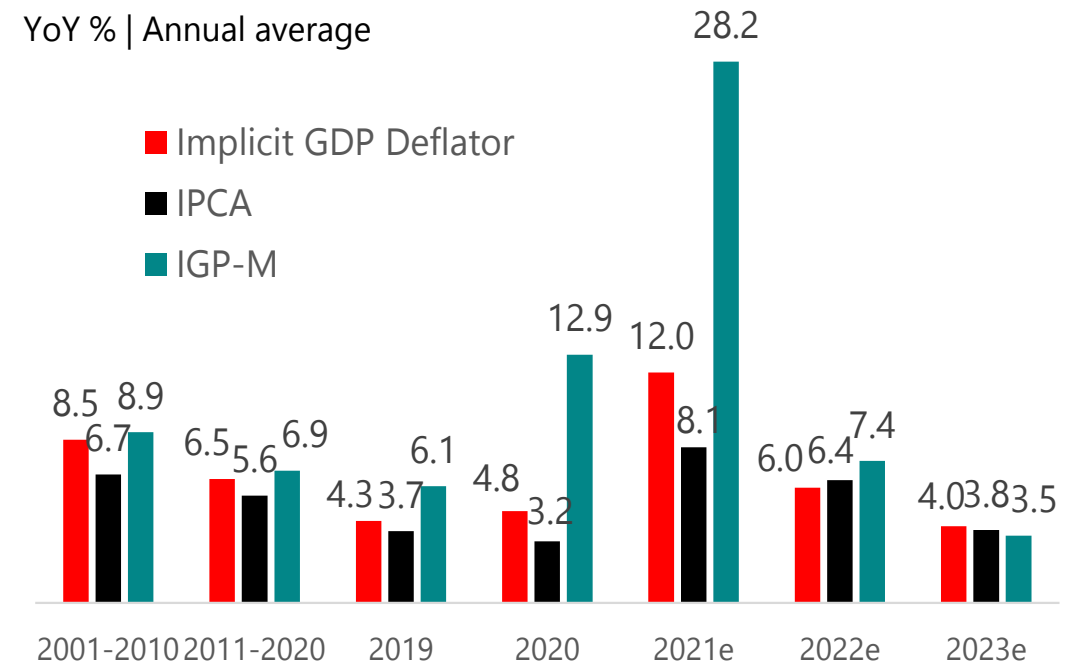
IPCA and GDP Deflator



Sources: IBGE, Santander.

IPCA, IGP-DI and GDP Deflator

YoY % | Annual average

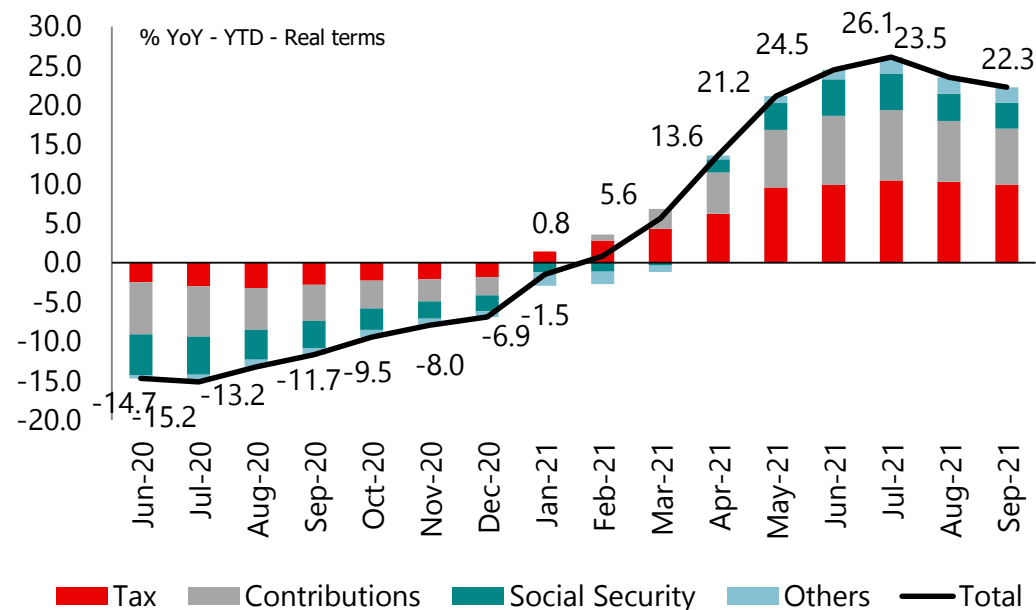


Sources: IBGE, FGV, Santander.

Revenues Impact – Inflation is Boosting Tax Collection in Federal and Regional Terms

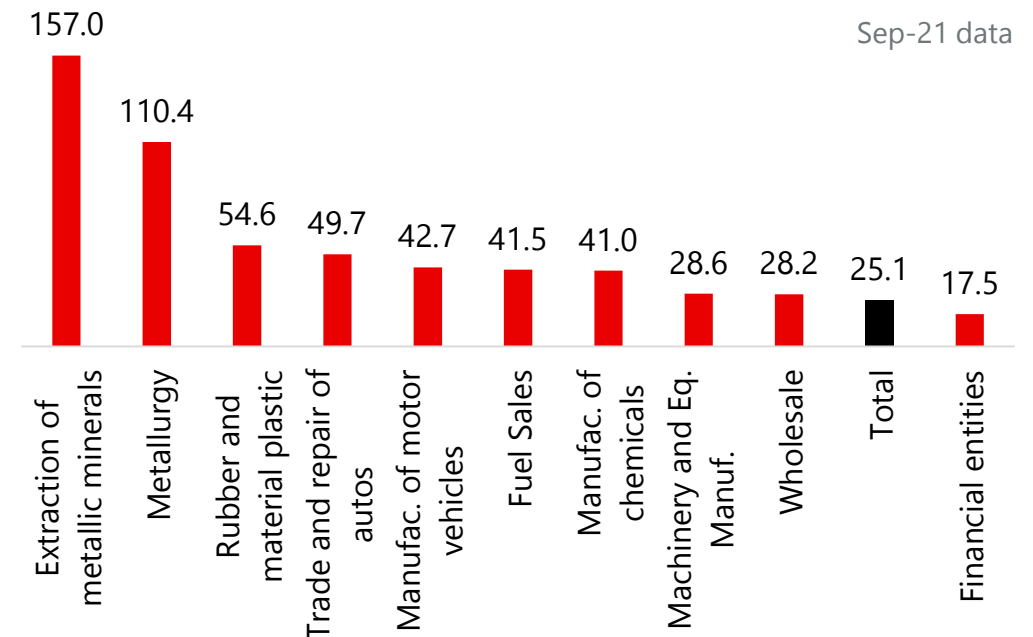
- We see a strong recovery in federal tax collection in recent months, mainly direct taxes linked to the business sector, which have posted good results recently. We can also observe that the increase in tax collection is highly correlated with sectors linked to the commodity boom, especially those related to metals.
- In our view, we expect revenue growth to slow down (still positive), for the following reasons: i) Greater basis for comparison compared to 2020 - with payment of deferrals in 2H20; ii) commodity prices losing steam; iii) normalization of the consumption basket - with more services (lower tax collection); iv) activity at a slower pace of growth after the crisis recovery.

Federal Tax Revenue: Year-to-date (%YoY)



Sources: Brazilian IRS, Santander.

Federal Tax Revenue by sectors YTD (%YoY)

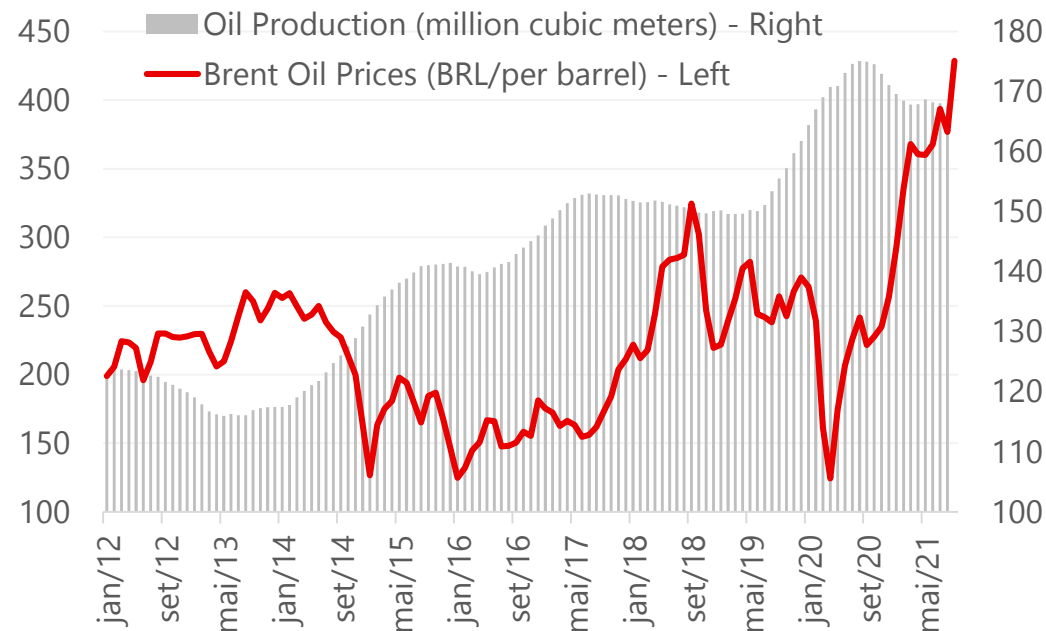


Sources: Brazilian IRS, Santander.

Revenues Impact – We also recently reviewed the royalties revenues

- Another important aspect was the recovery in royalty revenues. It increased BRL4 bn in September, on the heels of oil prices increase. In our last scenario revision, a key factor was the new royalty revenue estimates, owing to the recent price surge, mainly from oil and iron ore production. We forecast this revenue now at BRL90 billion, from BRL82 billion in September, which represents an increase of 66% compared to 2020 and 38.4% compared to 2019.

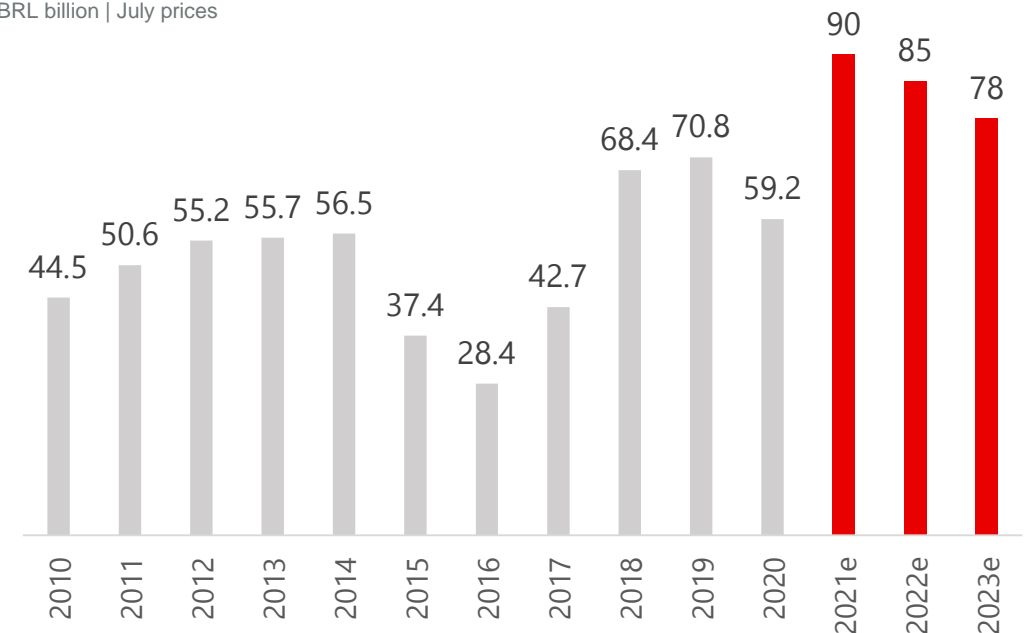
Oil Prices and Production



Sources: Bloomberg, ANP, Santander.

Revenues from Exploitation of Natural Resources

BRL billion | July prices

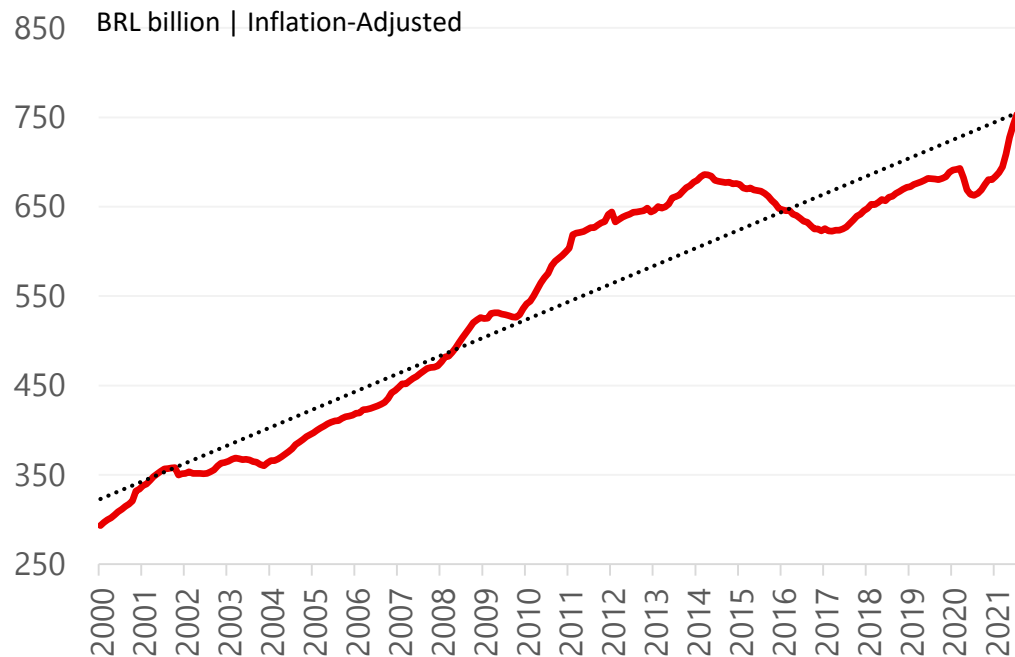


Sources: Bloomberg, Santander.

Revenues Impact – Inflation is Boosting Tax Collection in Federal and Regional Terms

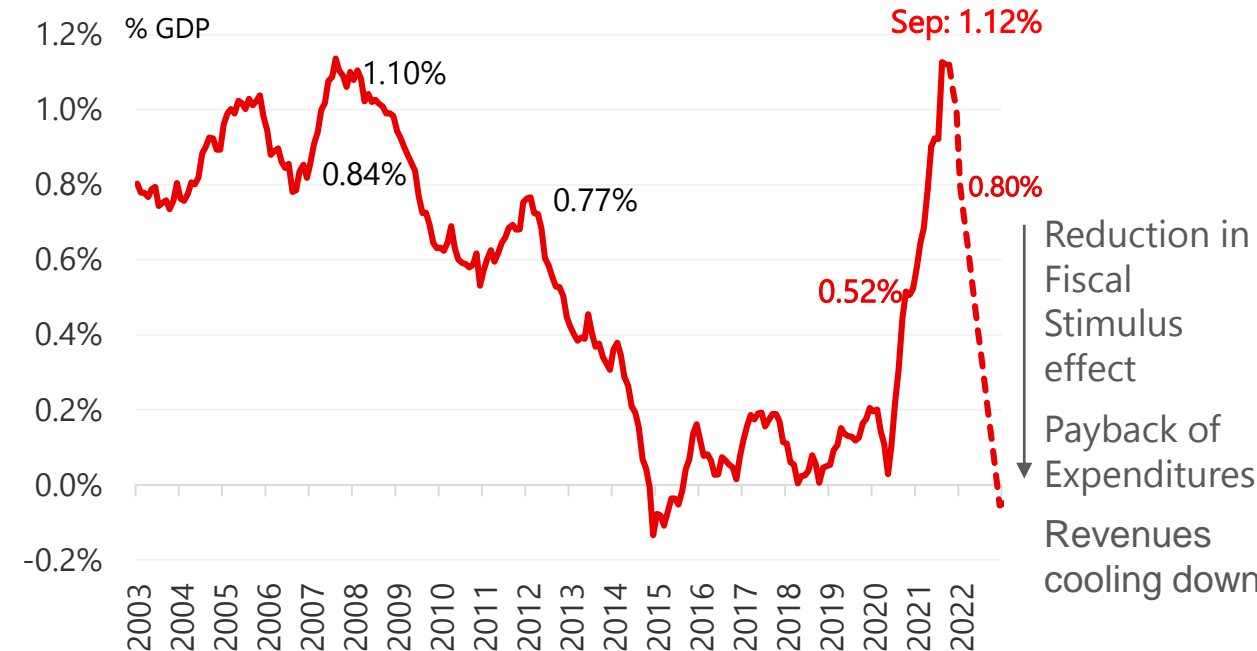
- In July, the regional governments' primary result continued to post positive numbers. The recent results were probably affected by the lagged effects of the 2020-21 fiscal stimulus on local economies, added to the effect of the price shock (terms-of-trade and inflation) on tax collection—and the activity recovery (formal sector) in the last few months.
- We believe that regional governments will face the challenge of reestablishing fiscal balance in the medium term after the end of fiscal and monetary stimuli, mainly, in our view, because of pressure to increase mandatory expenditures in the next year (for example, pressure to increase public servants' wages, after a period without a nominal increase).

Total Revenues 12m – Brazilian States



Sources: Confaz, Santander.

Regional Governments – Primary Result

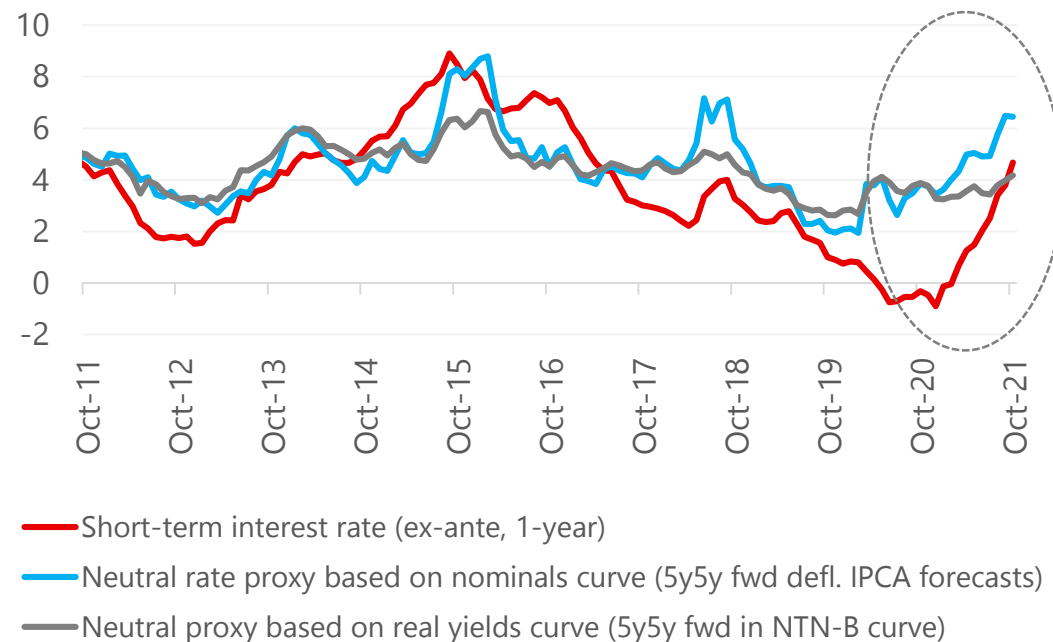


Sources: BCB, Santander.

On the other side, we see an increase in interest rates

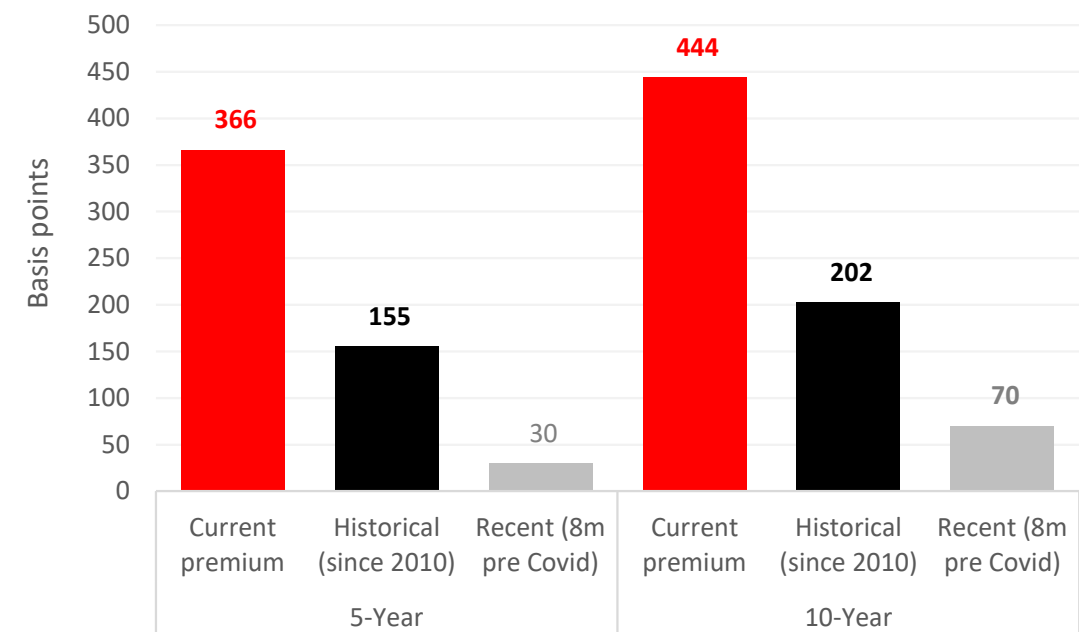
- As the BCB faces worsening inflation conditions and seek to curb expectations for the relevant policy horizons, we look for a faster and larger interest-rate adjustment in this cycle. We revised our Selic rate forecast for the end of 2021 to 9.25% (previously 8.25%). A possible decline to the neutral level (which we assume at 7.00%) is to take place only after 2023.
- Despite the improvement in the short-term fiscal numbers, the risk related to the fiscal consolidation remains elevated, in our view.

Proxies for Short- and Long-Term Interest Rate



Sources: Bloomberg, Anbima, Santander.

Current rise in risk premium



Sources: Bloomberg, Santander.

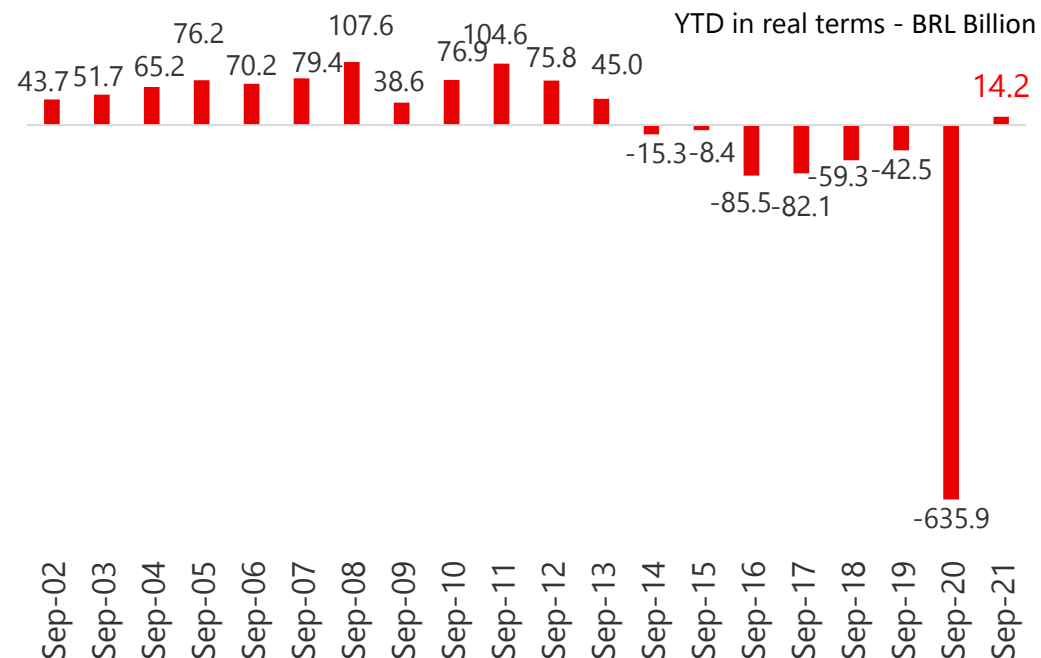
Fiscal Baseline Scenario – Primary Result and Simulations

06

Public Sector Primary Result Improving with the Inflation-effect

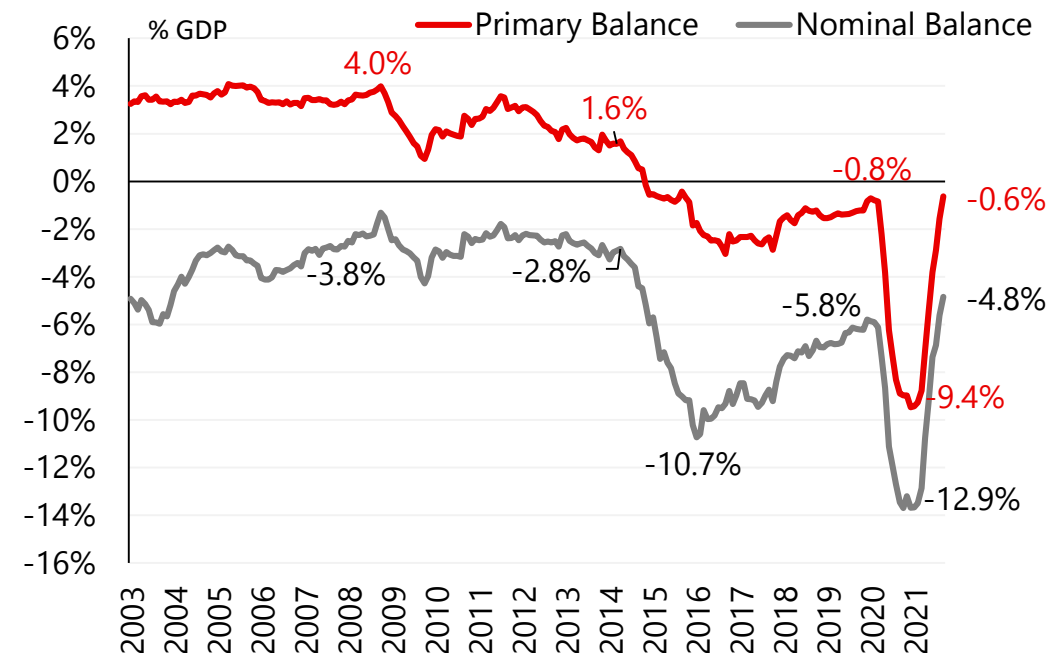
- In YTD terms, considering the surprising results for regional governments, the public sector reached a primary surplus of BRL14.2 billion (0.22% of GDP) in September, compared to a deficit of BRL636 billion (11.7% of GDP) in September 2020, affected by a massive fiscal stimulus during that year, and compared to -BRL42.5 billion (0.77% of GDP) in 2019.
- In the 12-month reading, the primary deficit reached BRL52.9 billion (0.6% of GDP) in September, compared to BRL130.3 billion (1.6% of GDP) in August, maintaining a downward trajectory after a sharp reduction in the fiscal stimulus in 2021 vs. 2020 (close to 9.2% of GDP summing up both years).

Public Sector – Primary Result



Sources: BCB, Santander.

Public Sector – 12m % GDP



Sources: BCB, Santander.

Fiscal - Pre-Pandemic Levels with a Bumpy Road Ahead

Central Government's Primary Balance												
Fiscal Items (% of GDP)	2019	2020	2021e	2022e	2023e	2024e	2025e	2026e	2027e	2028e	2029e	2030e
Total Revenue	22.1	19.7	21.3	21.0	21.2	21.6	21.8	21.7	21.7	21.7	21.7	21.6
Revenues Collected by the Federal Revenue Office	12.8	12.1	13.4	13.1	13.3	13.5	13.5	13.5	13.4	13.4	13.3	13.3
Net Social Security Revenues	5.6	5.4	5.1	5.0	5.0	5.1	5.1	5.2	5.2	5.2	5.2	5.1
Revenues Not Collected by the Federal Revenue Office	3.7	2.2	2.8	2.9	3.0	3.1	3.1	3.1	3.1	3.2	3.2	3.2
Transfers by Revenue Sharing	3.9	3.5	4.0	4.0	4.0	4.0	3.9	3.9	3.8	3.8	3.7	3.7
Net Revenue	18.2	16.2	17.4	17.0	17.2	17.7	17.8	17.9	17.9	17.9	17.9	17.9
Total Expenditure	19.5	26.1	18.6	18.3	18.3	18.2	17.8	17.4	17.1	16.7	16.3	16.0
Social Security Benefits	8.5	8.9	8.1	8.3	8.4	8.4	8.3	8.2	8.1	8.0	7.9	7.8
Payroll	4.2	4.3	3.8	3.7	3.6	3.6	3.5	3.4	3.3	3.2	3.1	3.0
Other Mandatory Expenses	2.6	9.7	3.7	3.2	3.2	3.1	2.9	2.8	2.7	2.6	2.5	2.4
Mandatory Expenses with Cash Control	4.1	3.2	3.0	3.1	3.1	3.1	3.0	3.0	2.9	2.9	2.8	2.8
Discretionary Expenses	2.2	1.5	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Central Government's Primary Balance	-1.3	-10.0	-1.3	-1.3	-1.1	-0.5	0.0	0.4	0.8	1.2	1.6	2.0
Public Sector Primary Balance	-0.8	-9.4	-0.5	-1.3	-1.1	-0.5	0.0	0.4	0.8	1.2	1.6	2.0
Nominal GDP (BRL billion)	7,407	7,448	8,743	9,389	9,852	10,384	11,054	11,766	12,525	13,332	14,192	15,106

Sources: National Treasury, Brazilian Central Bank, Santander.

→ **Main assumptions for the current baseline scenario:** our baseline macro scenario for 2021, 2022 and 2023. **After 2024:** (i) Potential GDP growth = ~1.5%; (ii) Neutral real interest rate = 4.0%; (iii) Long-term inflation = 3.0%, GDP deflator = 3.9%; (iv) Structural reforms in 2023 reducing mandatory expenses to maintain the discretionary expenses close to 1.2% of GDP; (v) Government will need to hire a lower number of public servants due to the digitalization of some public services; (vi) Pension reform will maintain the expenses almost stable in relation to GDP growth. We consider our new forecasts for judicial claims, the final estimate will depend on the decisions for the 2022 Budget onwards current decisions and legislation.

Fiscal Risks – Size Of The Fiscal Stimulus And Leftovers

- The total size of the War budget (2020) expenses totaled BRL524 billion. This year could reach ~BRL125 bn because extra-cap expenses in 2021.
- We anticipate that the government will maintain the expenditure in Vaccine Acquisition (as a 2021 Leftover – not considered in the spending cap) of BRL10 billion for 2022.

Expected 2021 – Extra-cap expenditure

Santander - Expected execution of Covid related expenditures - 2021	BRL billion
Emergency Aid (<i>PEC Emergencial</i>)	36.0
Emergency Aid extension (Aug-Oct)	25.3
PEC Precatórios Additional	10.0
Vaccine Acquisition (2020 Leftovers)	22.0
Health Expenditures	15.0
Pronampe 2021 (credit support for SMEs)	5.0
BEm 2021 (formal job support program)	11.7
TOTAL	125.0
Total (% of GDP)	1.4%
% of total forecasted by the Government (BRL150bn)	83.3%

Sources: National Treasury, Santander.

Tracking 2021 – Extra-cap fiscal expenditures

BRL Billion - Accumulated	Jul-21	Aug-21	Sep-21	Total Budgeted	Executed
Emergency Aid (MP 1.037 and 1.056/2021)	35.8	44.3	52.5	64.9	80.8%
Health expenditures	11.4	14.2	17.8	26.0	68.7%
BEm - Employment Program (MP 935/220 and MP 1.044/2021)	6.4	7.6	7.7	11.7	66.0%
Turism Infraestructure (MP 963/2020)	0.4	0.5	0.5	1.9	26.0%
Vaccine Acquisition (MP 994, 1,004 and 1,015/2020)	9.6	11.7	13.8	26.2	52.7%
Pronampe (credit support for SMEs) (MP 1,053/2021)	5.0	5.0	5.0	5.0	100.0%
Accumulated Total	68.7	83.2	97.3	135.6	71.7%

Last update: 10/06/2021

Sources: National Treasury, Santander

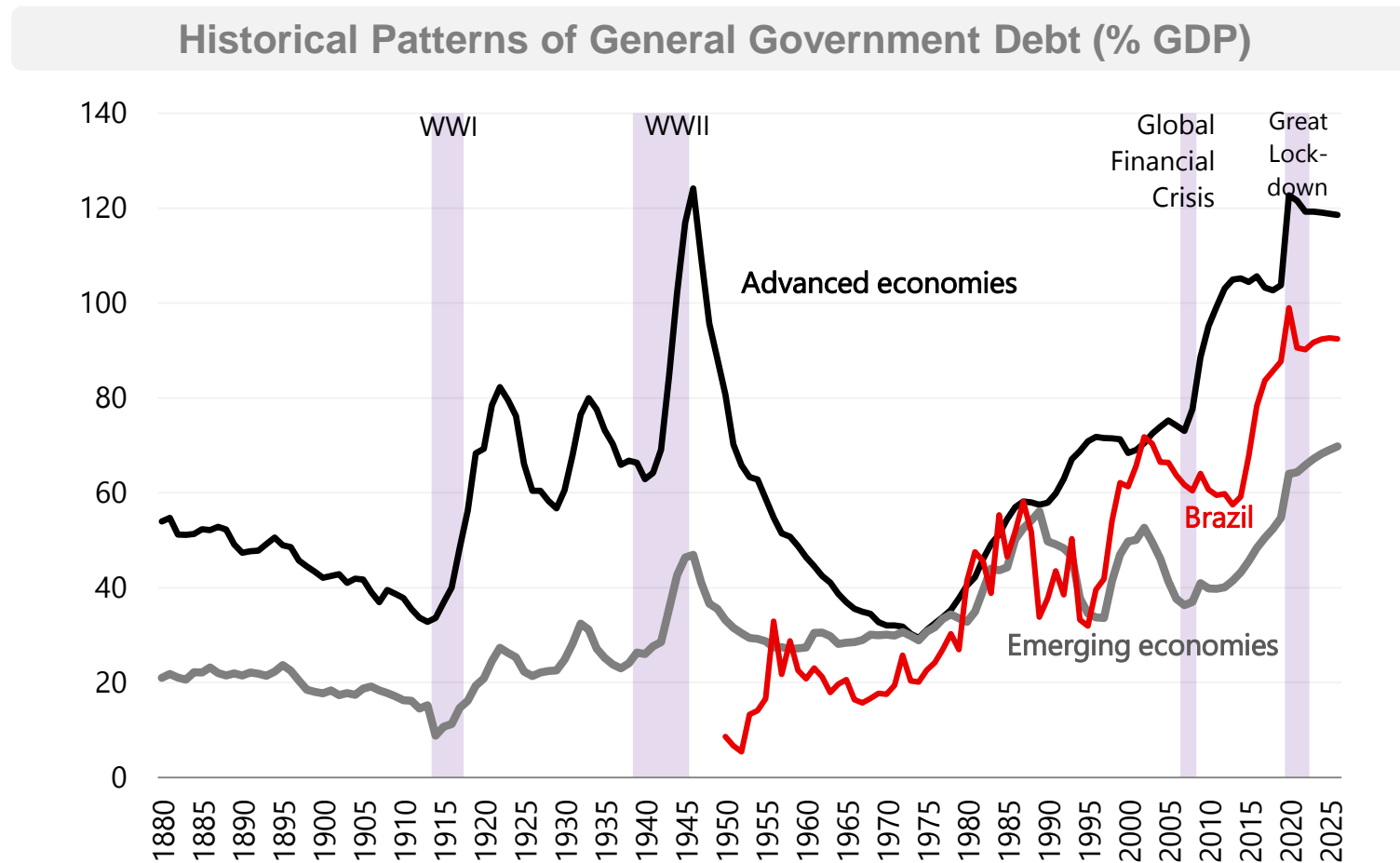
Includes Leftovers of War Budget (*Restos a pagar*)

Public Debt Scenario and Simulations

07

Brazilian gross debt approaches the level of advanced countries – International Comparison

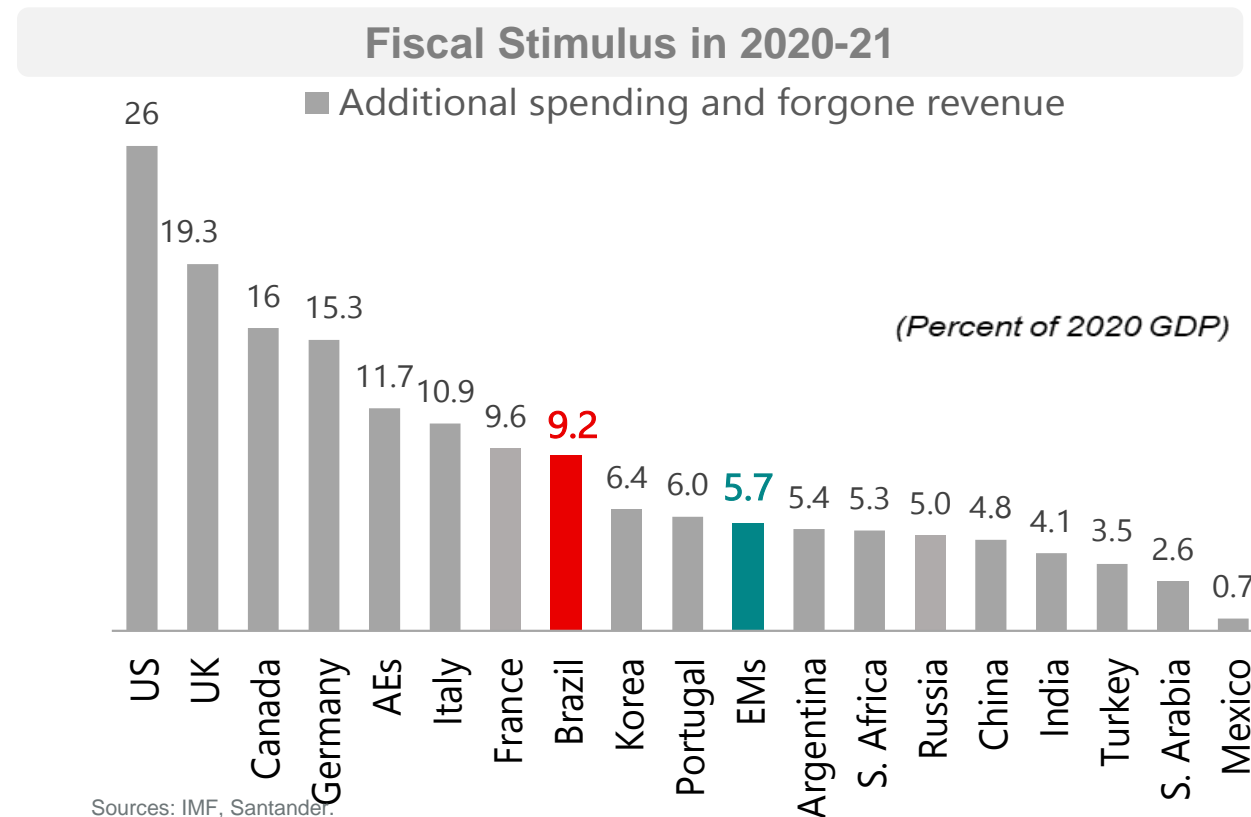
- Brazilian government finances registered an unprecedented deterioration in 2020, affected by the government's measures to mitigate the economic and health effects of the pandemic.



Sources: IMF, Santander.

Fiscal Monitor – IMF Scenario

- According to data from both 2020 and 2021, Brazil's fiscal stimulus reached 9.2% of GDP, higher than the 5.7% of GDP for the average of emerging economies (EM).
- In short, the fiscal outlook presented by the IMF is close to our fiscal scenario and reinforces the importance of both measures and reforms to guarantee the credibility of the fiscal consolidation.



Fiscal Accounts: Trajectories for the Brazilian Government Debt

- Public sector's primary balance (% GDP) required for the stabilization of the gross public debt-to-GDP ratio at **90%**
- We see the neutral interest rate hypothesis at 4.0%, this implies a larger primary surplus needed to stabilize the debt.
- Not considering the effects of the cyclical recovery, the long-term outlook will require a remaining 2.5-3.0% of GDP primary fiscal adjustment, just to stabilize the ratio debt-to-GDP around the higher post-pandemic level of ~90% of GDP.

Current situation:

- Real interest rate (ex-ante) 1-year: ~4.7%,
- GDP is expected to grow 4.9% in 2021

Liquidity reserves up to 11 months of debt maturities

Increase in debt cost (Selic + IPCA)

Steady-state:

According to our hypothesis:

- Real interest rate at +4.0%
- Potential GDP at +1.5%,
- The primary surplus must reach 1.8-2.2% of GDP to maintain the gross debt stable.

		Real Interest Rate							
		-1.0%	0.0%	1.0%	2.0%	2.5%	3.0%	4.0%	5.0%
GDP Growth	1.0%	-1.8	-0.9	0.0	0.9	1.3	1.8	2.7	3.6
	1.5%	-2.2	-1.3	-0.4	0.4	0.9	1.3	2.2	3.1
	2.0%	-2.6	-1.8	-0.9	0.0	0.4	0.9	1.8	2.6
	2.5%	-3.1	-2.2	-1.3	-0.4	0.0	0.4	1.3	2.2
	3.0%	-3.5	-2.6	-1.7	-0.9	-0.4	0.0	0.9	1.7
	3.5%	-3.9	-3.0	-2.2	-1.3	-0.9	-0.4	0.4	1.3

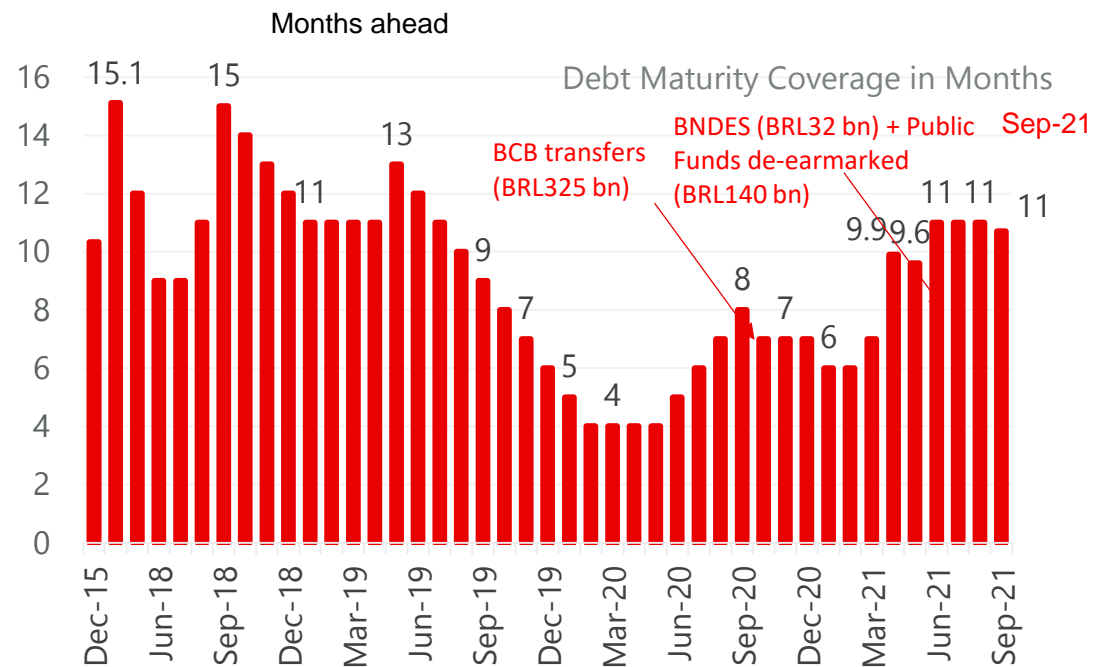
Debt Management

08

Treasury's Cash Position Improved in the Last Few Months with Larger Auctions

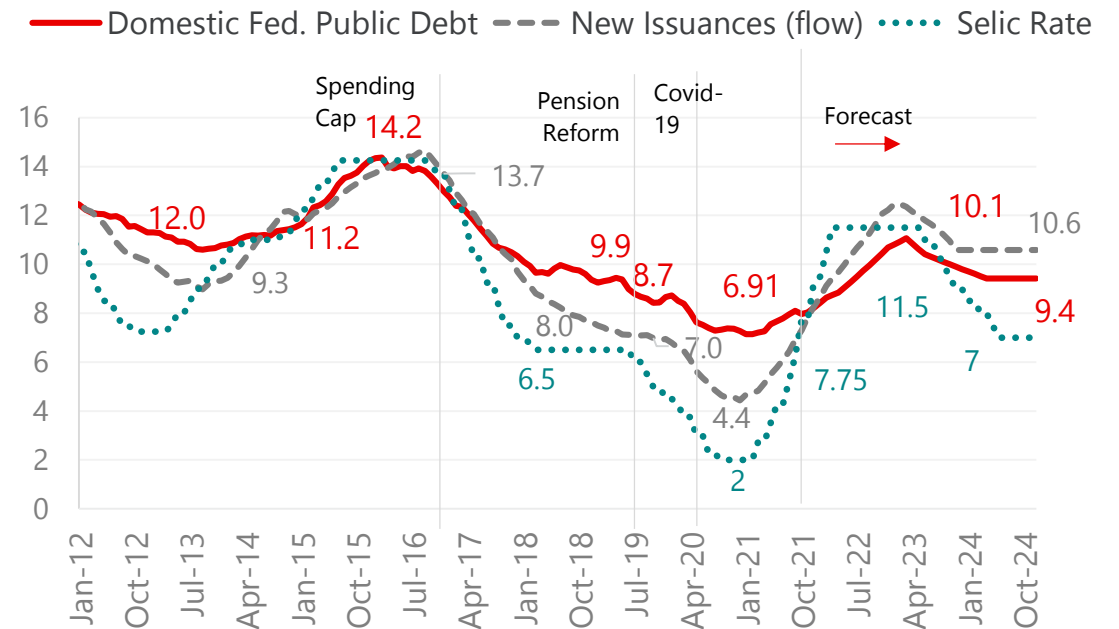
- With debt shortening it is important to keep the level of the liquidity cushion at comfortable levels.
- We observe an increase in the cost of debt issuance (part due to Selic rate and part long maturity issuances – especially with inflation-linked bonds). In the short-run the cost level of new issuances is still below the outstanding debt average cost, yet this should reverse ahead.

Liquidity cushion coverage of domestic debt



Sources: National Treasury, Santander.

Average cost of Federal Debt - 12 months – (%)

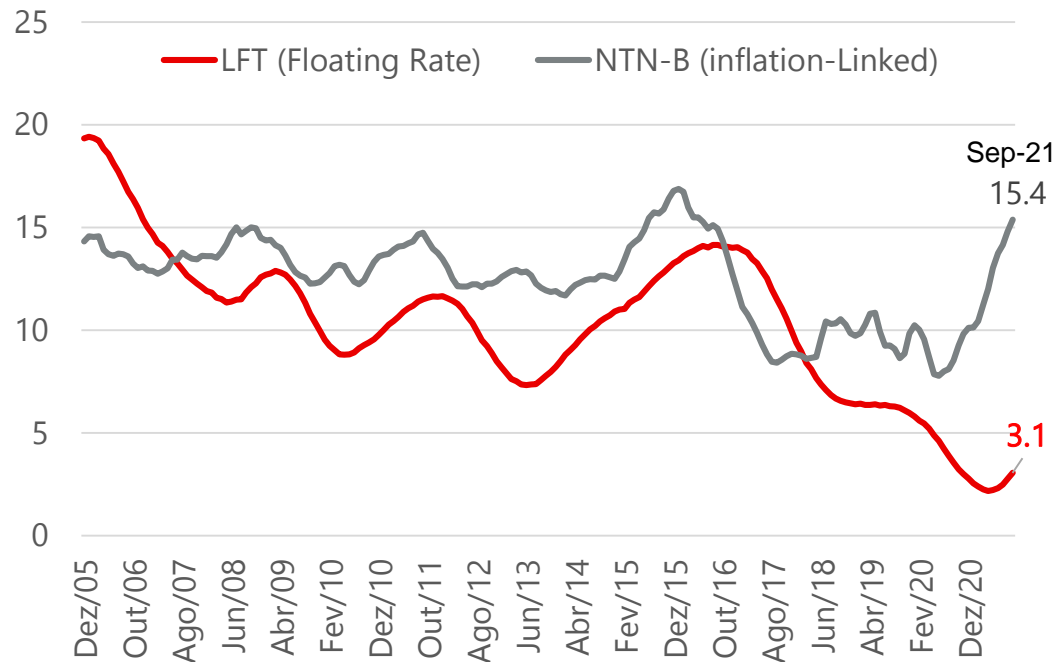


Sources: National Treasury, Santander.

At the margin there is a increase in debt cost related to Selic and Inflation

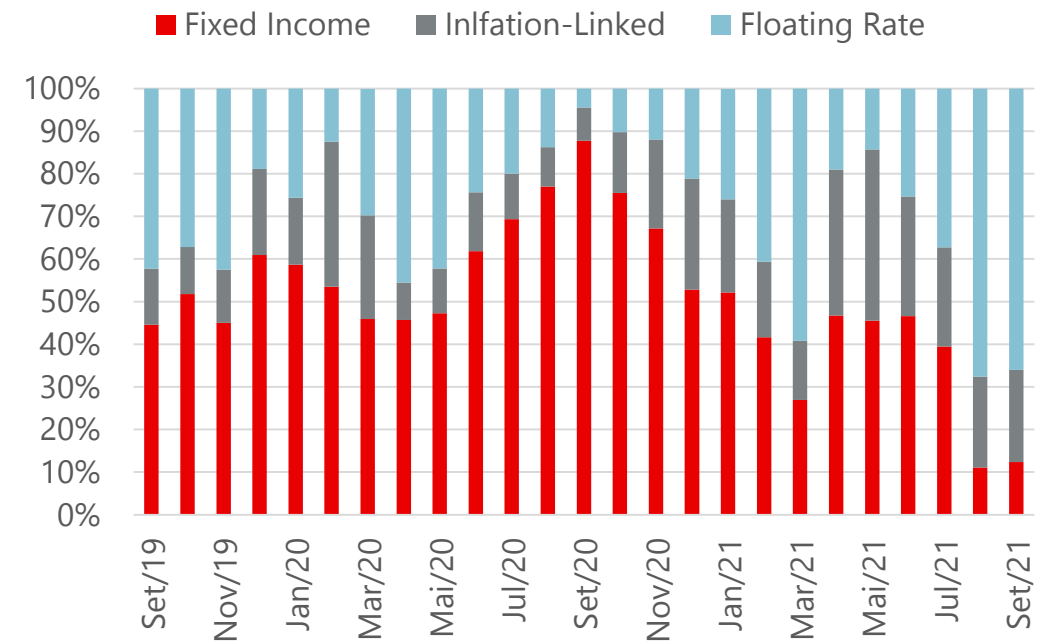
- The debt cost continued to rise, due to both inflation and Selic increase. The average cost of the outstanding debt accumulated in 12m rose to 7.79% (from 7.55% in August). New issuances cost rose to 6.9% p.y, +0.5p.p from August.
- The NTN-B (inflation-linked bonds) cost in the last 12m rose to 15.4% p.y. (+5.3pp since Jan-21). The cost of LFT (floating rate) in 12m increased to 3.1% (from 2.55% in January), the Selic increase (currently at 6.25%) could add an additional pressure in debt costs in coming months.

Average Debt Cost in the last 12 M (Accum.)



Sources: National Treasury, Santander.

Participation in total issuances (%)

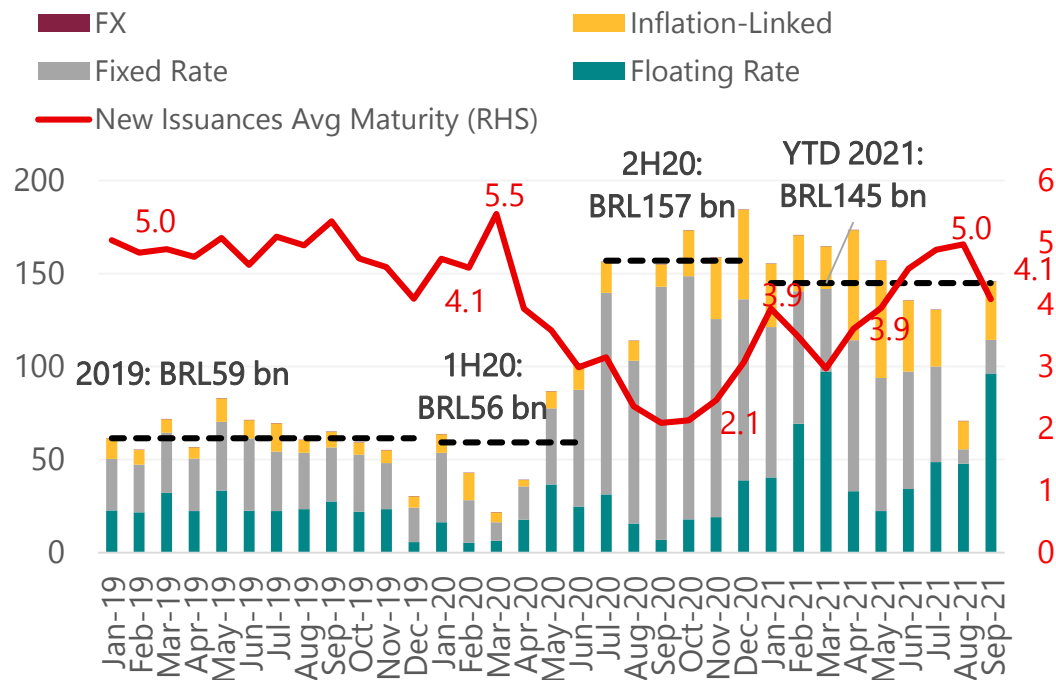


Sources: National Treasury, Santander.

Fiscal – The Increase in Selic Rate Will Pressure the Debt Issuances

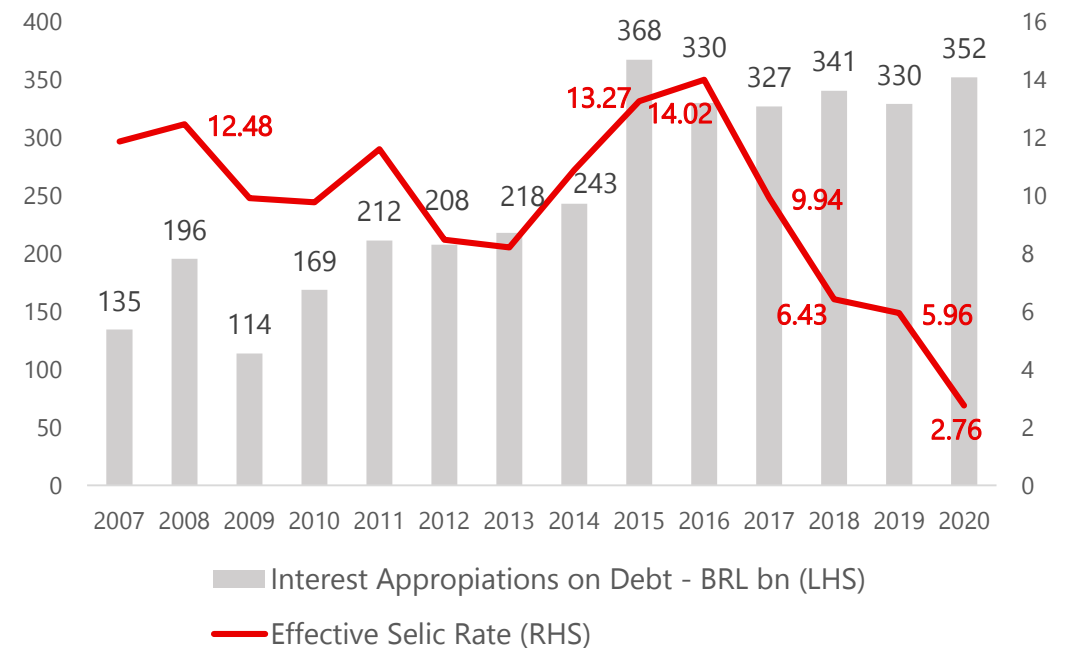
- Market conditions will be important for new debt issuances. Weekly bond issuances reached ~BRL34.1 bn until September, yet above to a required financial need until the end of the year of ~BRL16.8bn/week.

Treasury Issuances



Sources: National Treasury, Santander

Selic Rate and Debt

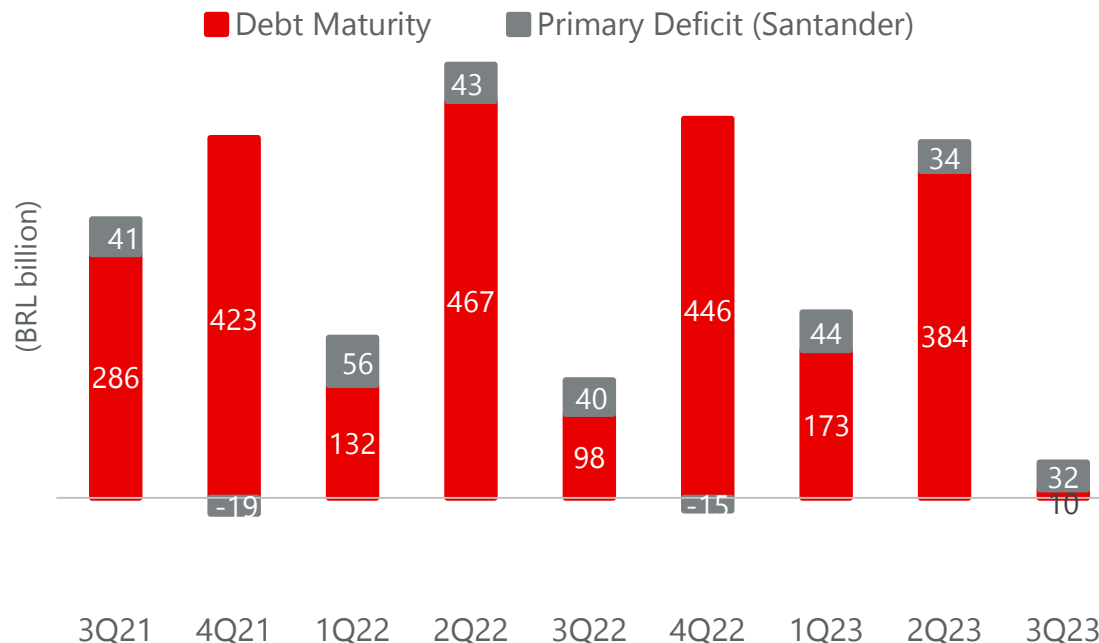


Sources: BCB, National Treasury, Santander.

Fiscal – The debt is at a higher level and with a shorter maturity

- Despite the increase in liquidity reserves the debt maturity level is still challenging. Structural reforms will help to increase debt maturity and reduce the primary deficit.

Debt maturity - (BRL billion)



Sources: National Treasury, Santander

Profile by categories - (BRL billion)

Quarter	Fixed Rate	Floating Rate (selic)	Inflation-Linked	FX-Exchange	Other	Total
4Q21	267.7	-	15.0	-	3.7	286.4
1Q22	133.9	260.0	24.1	3.7	1.2	422.9
2Q22	116.6	-	14.6	-	1.3	132.5
3Q22	124.2	165.6	172.1	3.5	1.1	466.6
4Q22	81.4	-	14.3	-	2.8	98.5
1Q23	263.2	159.7	18.7	3.4	0.6	445.6
2Q23	0.0	0.0	172.0	0.0	1.4	173.4
3Q23	156.7	204.8	18.3	3.2	1.2	384.2
4Q23	0.0	0.0	9.1	0.0	0.8	9.9

Sources: National Treasury, Santander.

MACRO SCENARIO: Forecasts

Macroeconomic variables		Previous		Current
GDP (%)	2021E	5.1	↓	4.9
	2022E	1.7	↓	1.5
	2023E	1.0	↓	0.8
IPCA (%)	2021E	8.5	↑	9.0
	2022E	4.3	↑	4.7
	2023E	3.3	→	3.3
Selic Rate (% end of period)	2021E	8.25	→	8.25
	2022E	8.50	↑	9.00
	2023E	7.00	→	7.00
FX Rate - USDBRL (end of period)	2021E	5.25	↑	5.35
	2022E	5.55	→	5.55
	2023E	5.20	→	5.20
Current Account Balance (% of GDP)	2021E	0.1	↓	0.0
	2022E	-0.6	↑	0.0
	2023E	-1.7	↑	-1.6
Primary Fiscal Balance (% of GDP)	2021E	-1.3	↑	-0.5
	2022E	-1.0	↓	-1.3
	2023E	-0.8	↓	-1.1
Gross Public Debt (% of GDP)	2021E	79.7	↑	80.7
	2022E	82.2	↑	83.8
	2023E	85.6	↑	87.8

Sources: IBGE, FGV, The National Treasury Secretariat, BCB and Santander.

- The forecasts refers to our latest Scenario Review
- "SIGNS OF NORMALITY IN PUBLIC HEALTH, EVIDENCE OF RISKS IN FISCAL POLICY"
- (sent on October 21, 2021)
- For the full report click on the link:
<https://bit.ly/Std-scenreview-oct21>

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