



Brazil Macro | April 2021

FX rate & Balance of Payments

Jankiel Santos*
jankiel.santos@santander.com.br
+5511 3012-5726

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SUMMARY

- International environment should continue to be relatively constructive on the heels of favorable commodity prices, bountiful liquidity in advanced economies and the progress in the immunization plans around the globe. However, prospects for the start of the monetary tapering in the US should push the DXY index up late in 2021 and trigger some correction in financial asset prices.
- The reintroduction of an emergency aid program in 2021 in tandem with the slow progress in the reformist agenda and the complex political environment should keep market participants skeptical about the trajectory of the Brazilian public indebtedness and limit the room for the BRL to strengthen this year. Then, anxiety with the presidential race should add to these concerns and lead the BRL to weaken during 2022.
- Positive prospects for the international trade flow, favorable levels for commodity prices, a weak currency and the gradual economic recovery for the Brazilian economy should continue to lead export proceeds to outpace import outlays and to curb remittances of profits & dividends and tourism outlays. Hence, we expect the current account balance to register surpluses in 2021 and 2022, which is a rather unusual situation for an emerging economy.
- As for the financial account, we expect some recovery in the volume of direct investments in the country, as the immunization program in the country rolls out and allows the economy to head toward a more normal situation. However, remaining financial items may refrain from flowing into the country amid higher uncertainty on the fiscal and political fronts, thus counterbalancing the current account surpluses.

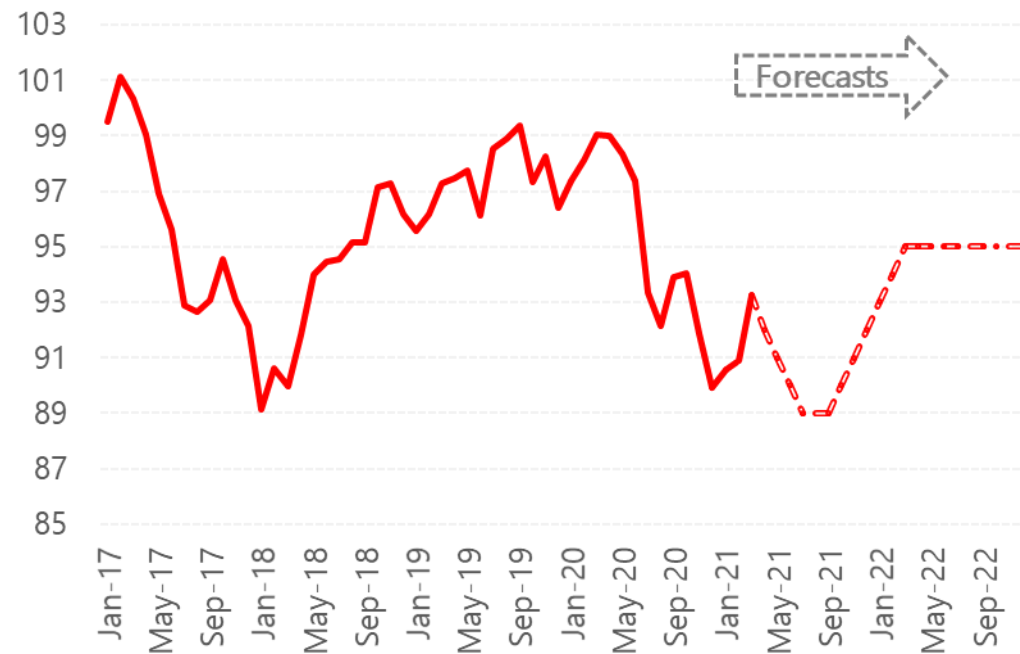
FX rate

02

A RELATIVELY CONSTRUCTIVE GLOBAL (LIQUIDITY) ENVIRONMENT

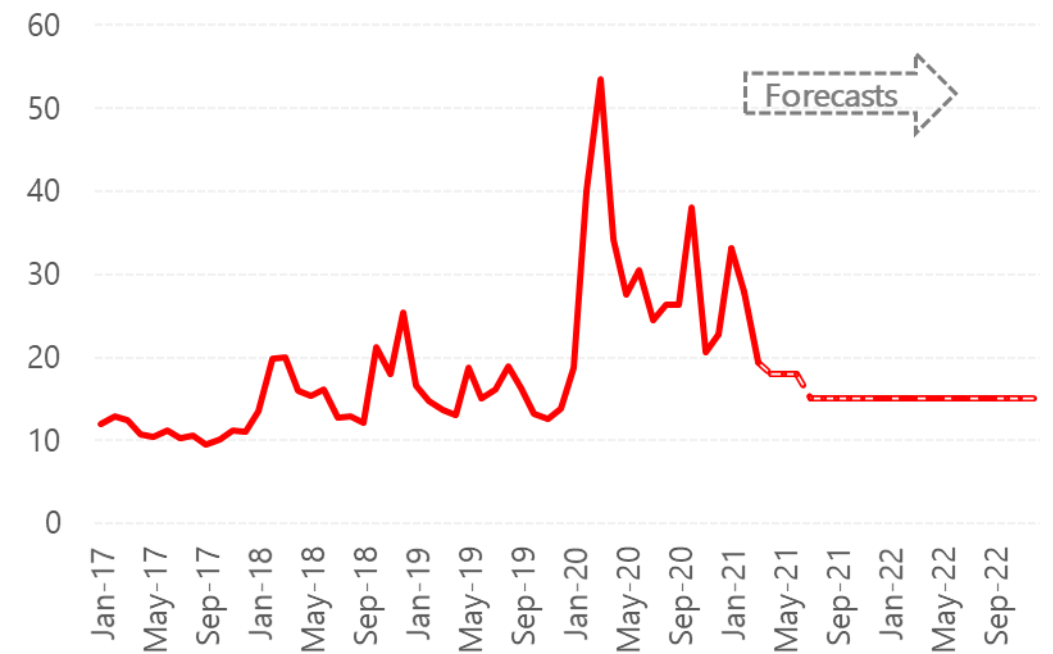
- Although we expect some reversal of the DXY Index late in 2021 on the back of prospects for the beginning of a monetary tapering in the US, we don't believe the move should leave the level of risk aversion among market participants to increase.

DXY Index (1973=100)



Sources: Bloomberg, Santander.

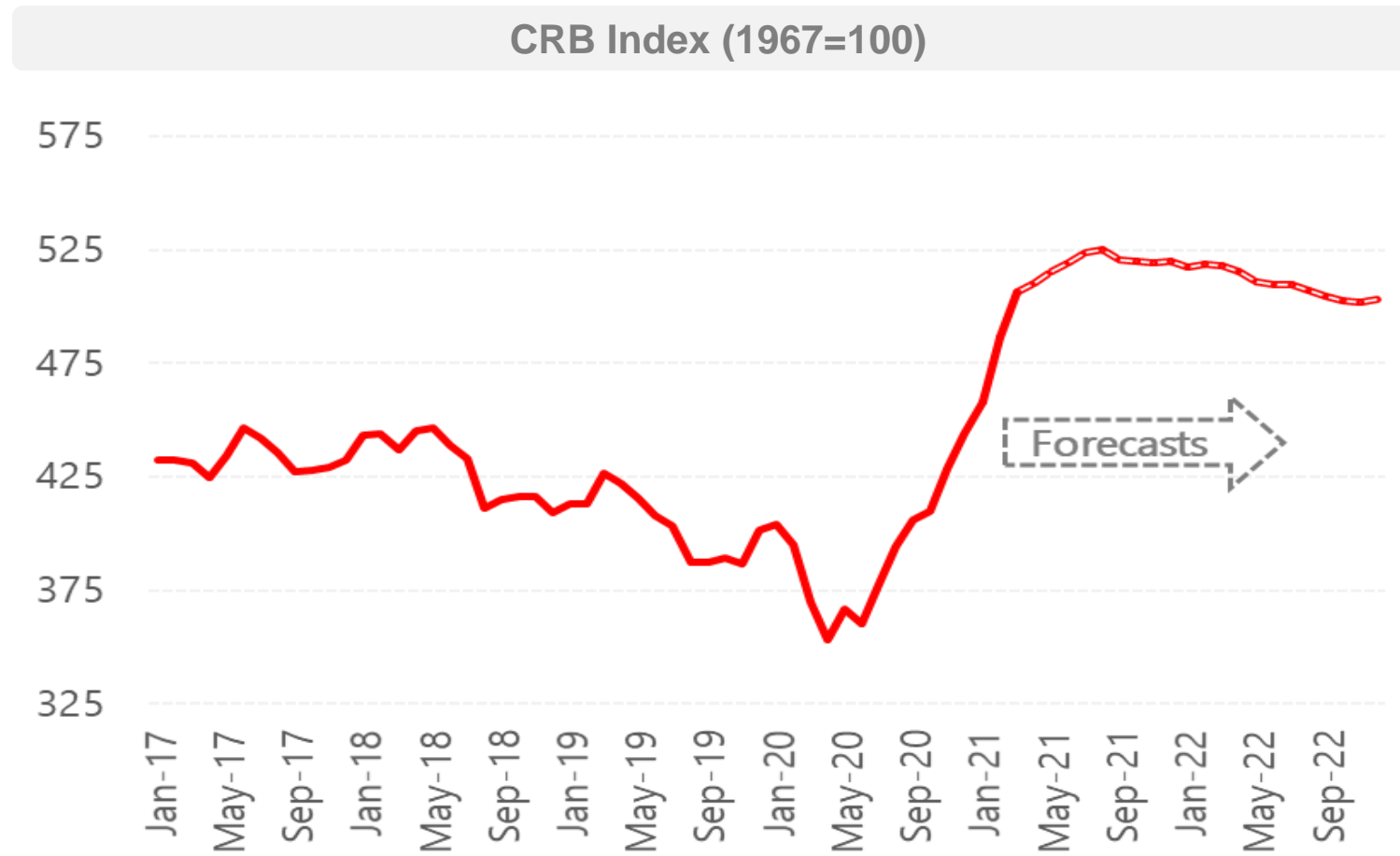
VIX Index (% pa)



Sources: Bloomberg and Santander forecasts.

QUITE FAVORABLE LEVELS

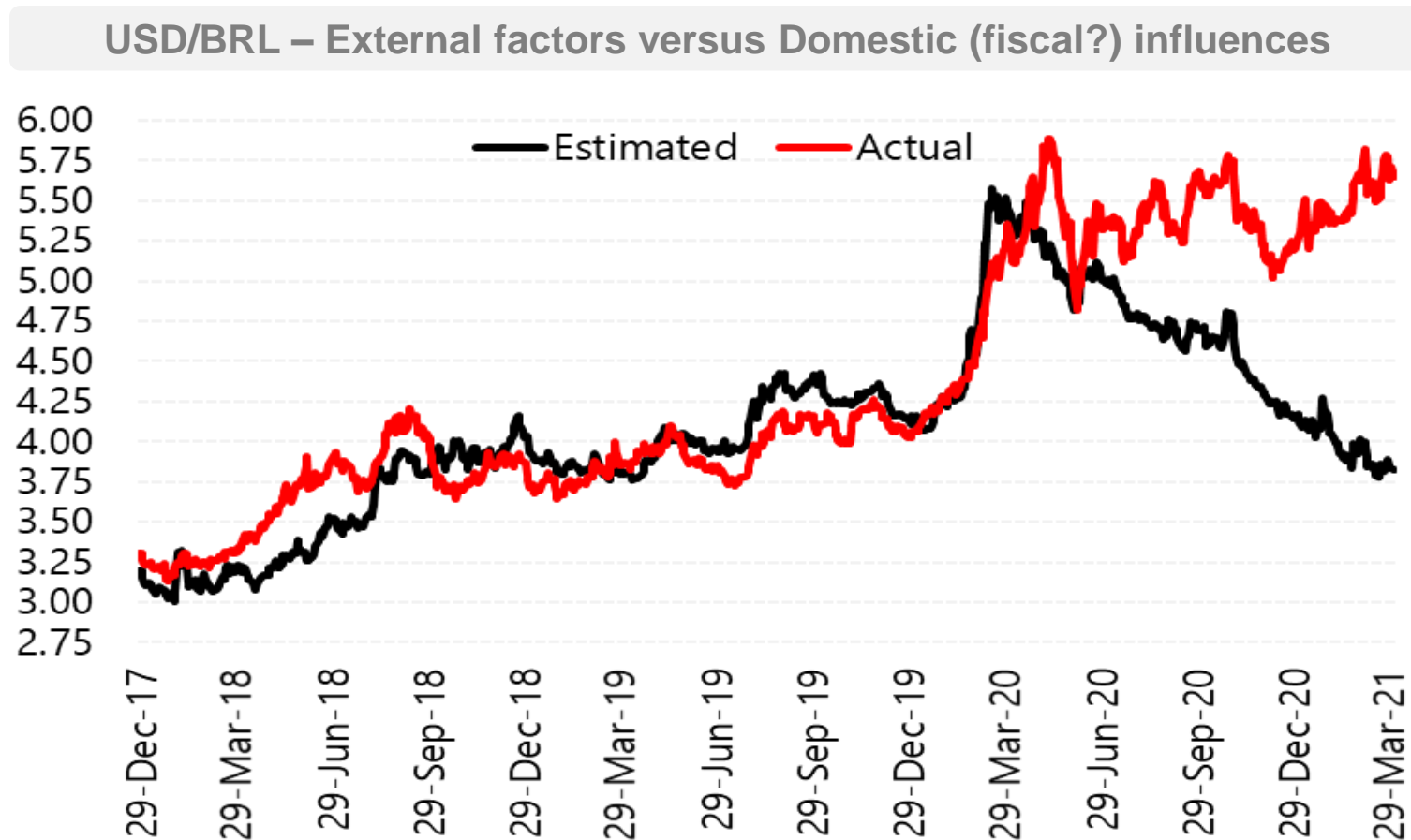
- Bounteous liquidity conditions, the seek for stock replenishment and the resumption of economic growth around the globe should support commodity prices at high levels, but we expect the US monetary tapering to ignite some correction during 2022.



Sources: Bloomberg, Santander.

A SIGNIFICANT RISK PREMIUM...

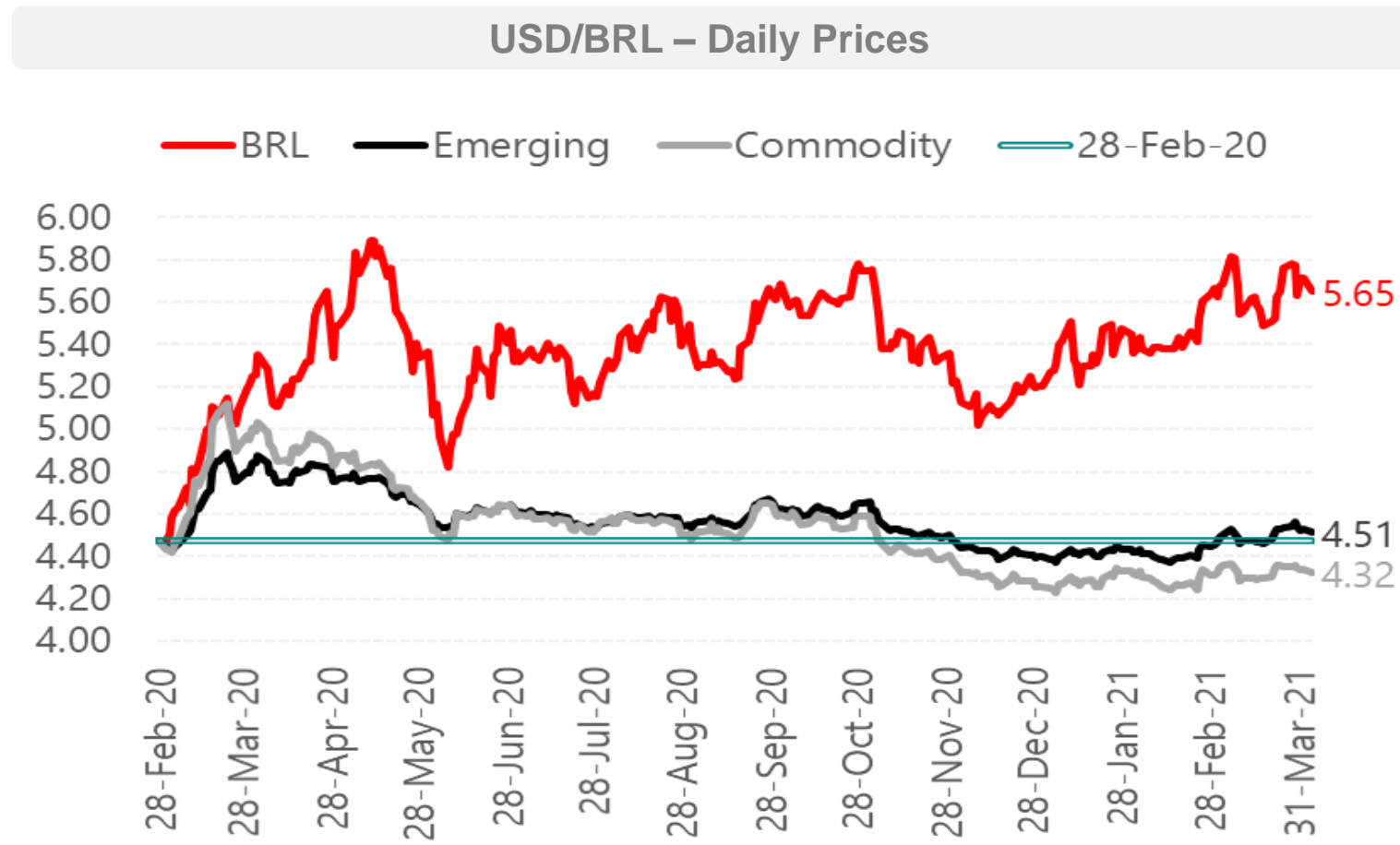
- Until mid-July, the BRL responded in a relatively close way to the influences of variables previously presented. However, as the skepticism regarding fiscal dynamics has increased lately, the Brazilian currency has decoupled from its main 'fundamentals'.



Sources: Bloomberg, Santander .

... NOT SEEN IN MANY OTHER CURRENCIES

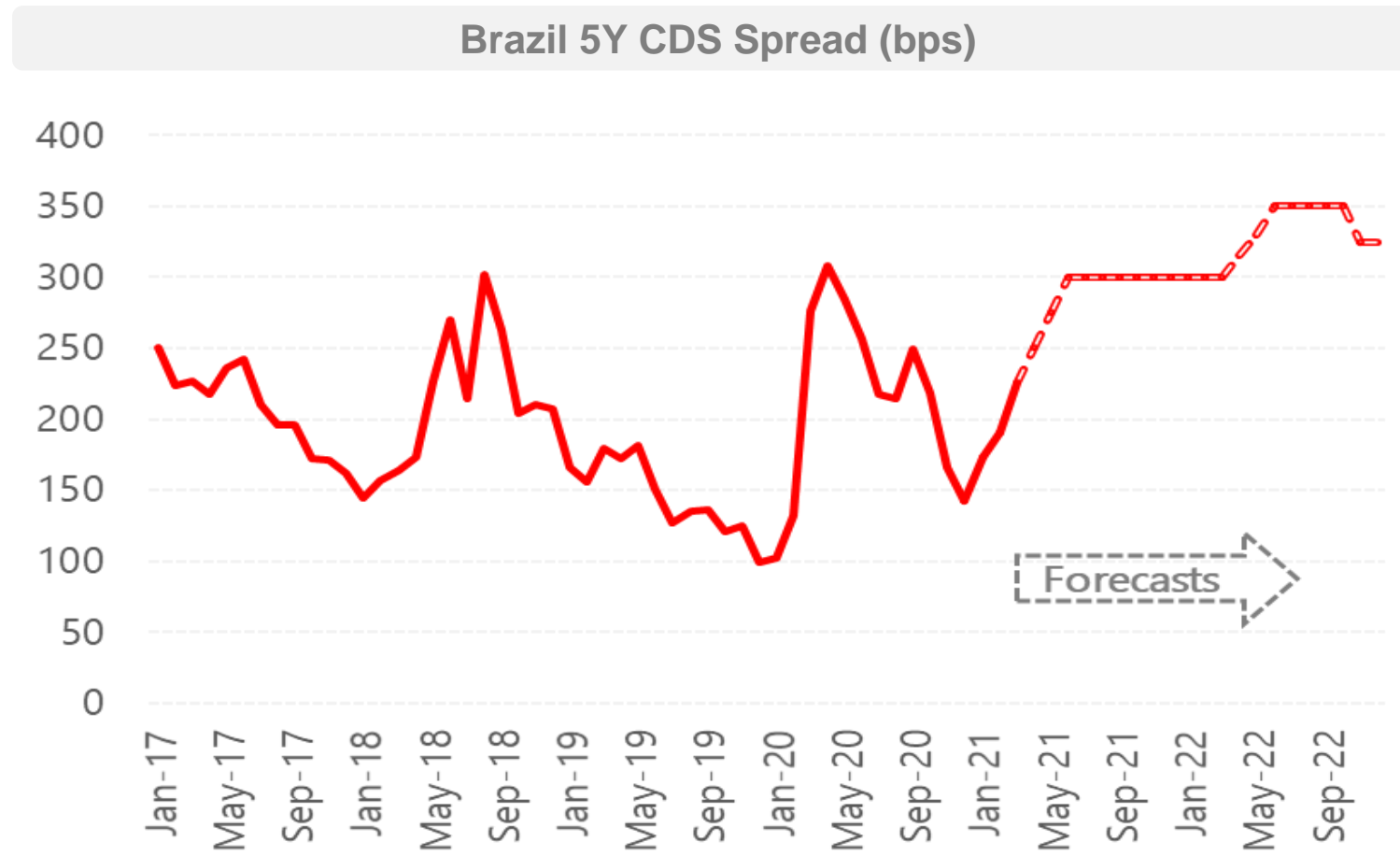
- The USD/BRL pair would be trading at pre-pandemic levels if it had followed the average change of emerging currencies (or stronger, according to currencies influenced by commodity prices).



Sources: Bloomberg, Santander .

HIGHER RISKS...

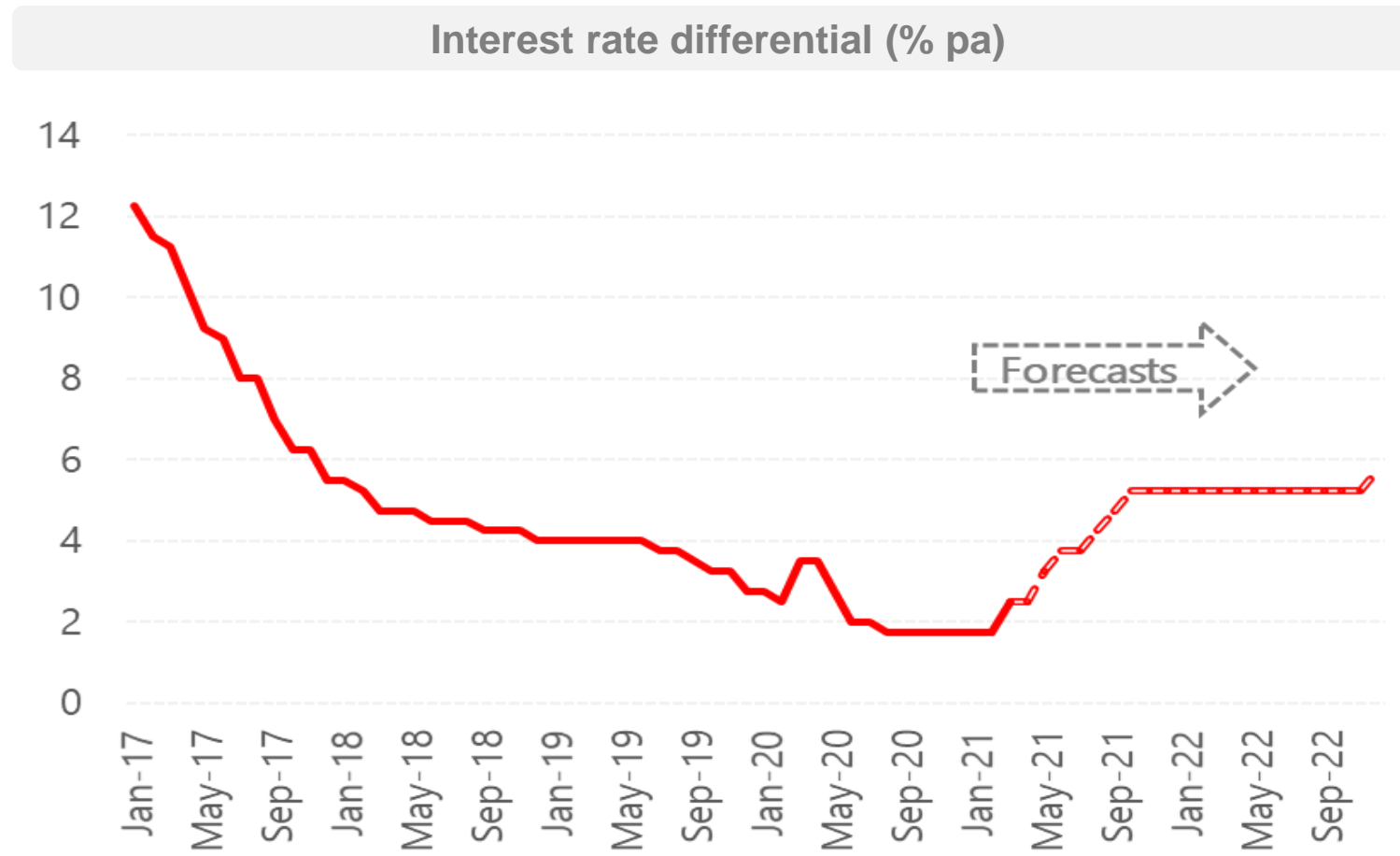
- The reintroduction of an emergency aid in 2021 has weighed on market participants' confidence and the approval of triggers to curb public outlays has just partially offset that influence. Then, the polarized presidential race we expect to witness in 2022 should lead to a new wave of uneasiness.



Sources: Bloomberg, Santander.

... HIGHER YIELDS

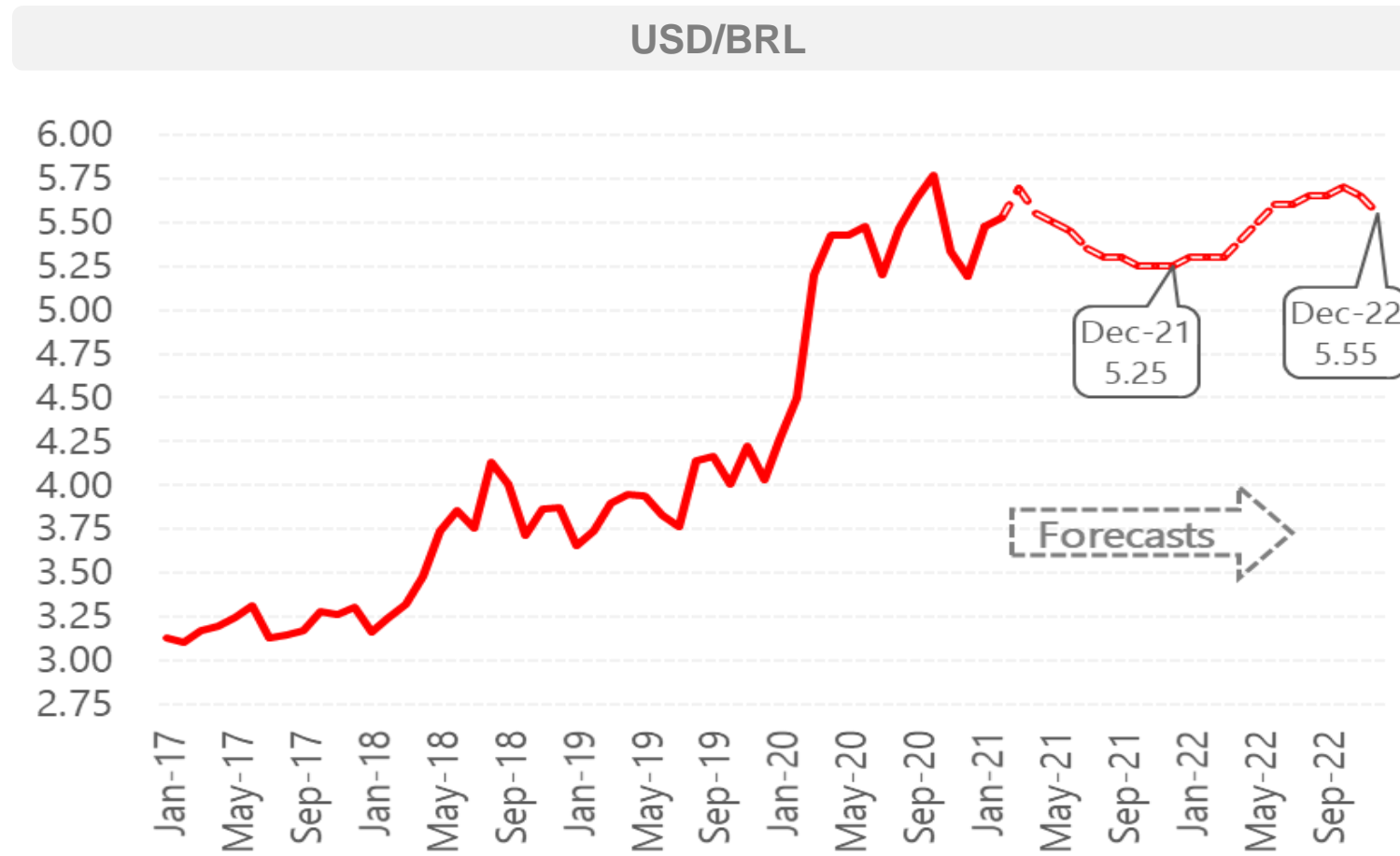
- Negative inflation surprises in the short term, less sanguine inflation expectations and a riskier fiscal outlook should lead the Brazilian Central Bank to anticipate the beginning of the monetary policy normalization.



Sources: Bloomberg, Santander.

LIMITED ROOM FOR STRENGTHENING

- The constructive international environment and the tighter monetary grip should partially offset the weakening pressure that higher sovereign risks and larger uncertainty with the fiscal policy conduct are going to exert over the BRL.



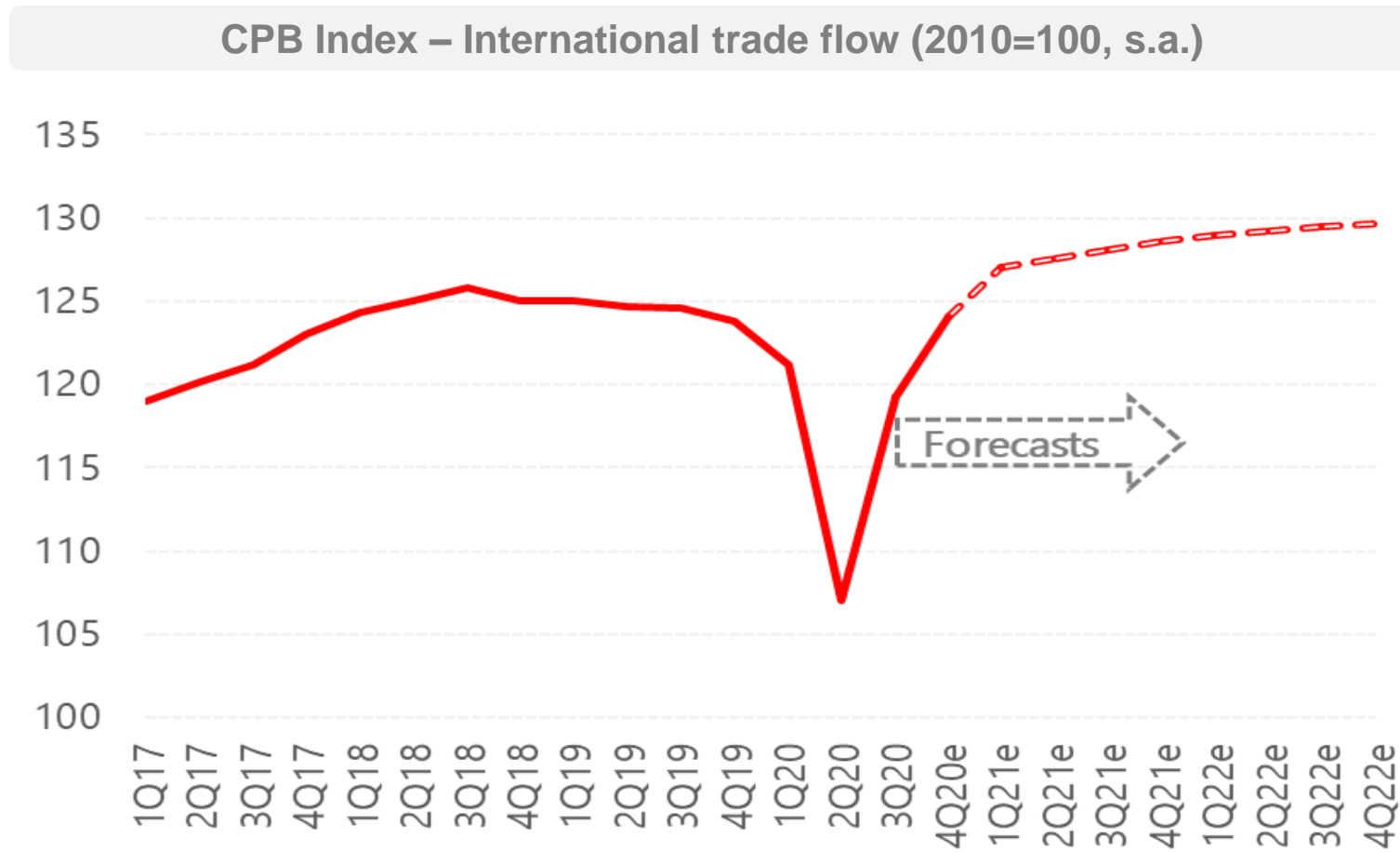
Sources: Bloomberg, Santander.

Balance of
Payments

03

A SIMILAR PLUNGE, BUT A FASTER (INITIAL) RECOVERY

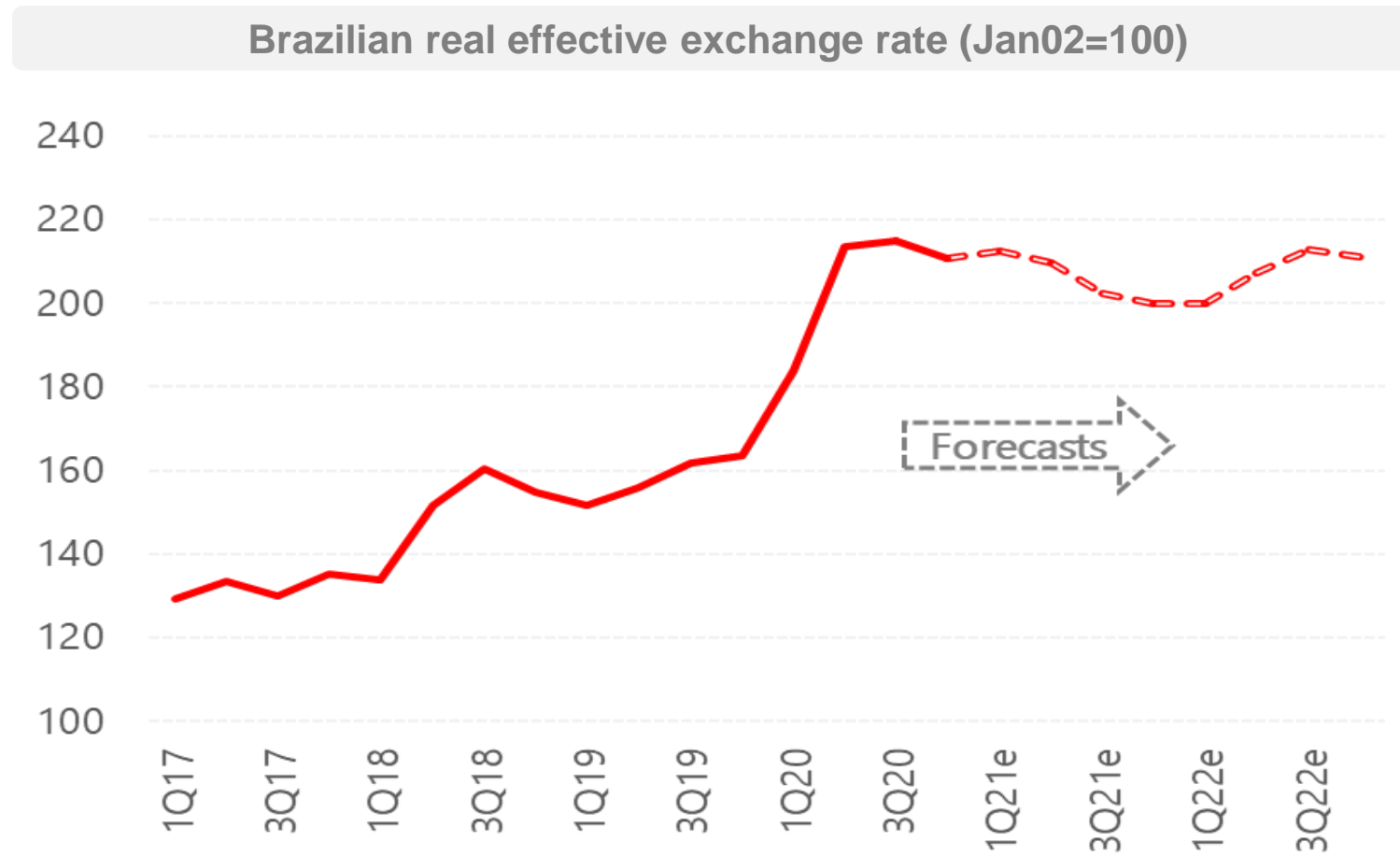
- The initial drop observed in international trade flows in 1H20 nearly matched the one observed in the 2008 crisis, but recent data indicates they have got back to their pre-pandemic levels and they should continue to grow—yet at a more gradual fashion.



Sources: Bloomberg, Santander.

WEAKER FOR LONGER

- Though higher than previously thought, we do not expect inflation to skyrocket, which means the nominal weakening of the BRL should, in fact, turn into an effective devaluation of the currency.

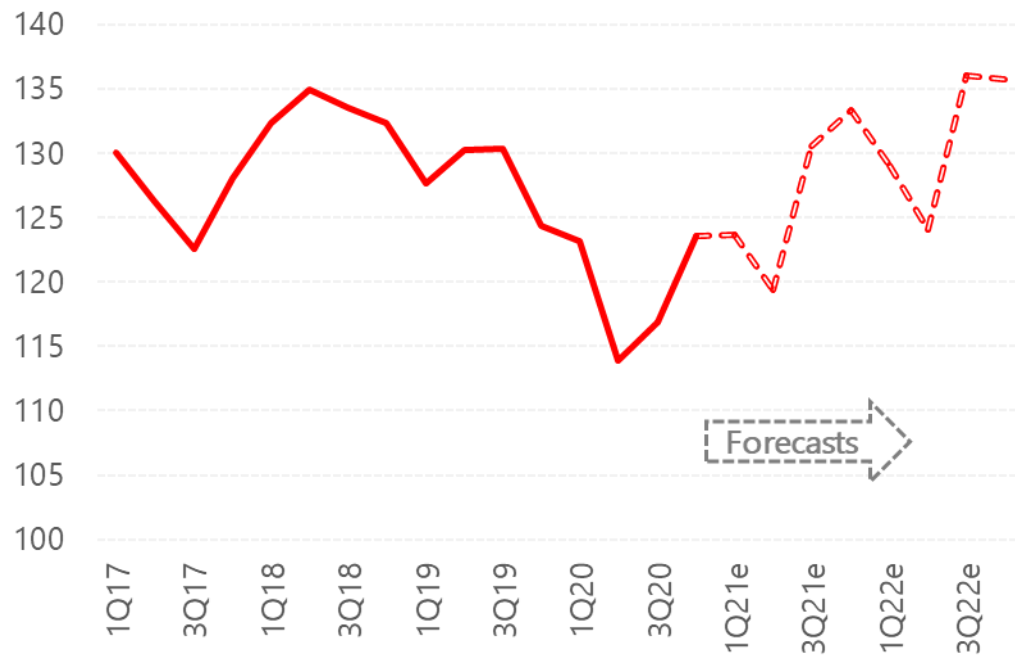


Sources: Bloomberg, Santander.

FURTHER IMPROVEMENTS IN TERMS OF TRADE

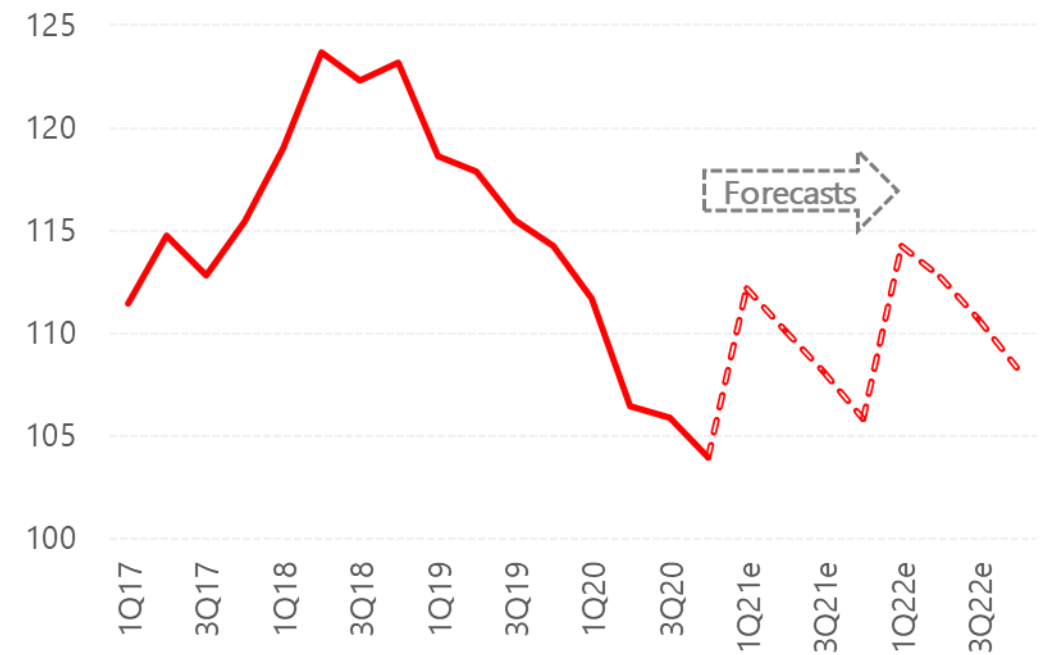
- Given our expectation of an extension in the bull market for commodities (beneficial for export prices) and the high global level of idleness in the industrial sector (detrimental to import prices), we judge the Brazilian terms of trade should continue to improve.

Export price index (2006=100)



Sources: FUNCEX, Santander.

Import price index (2006=100)

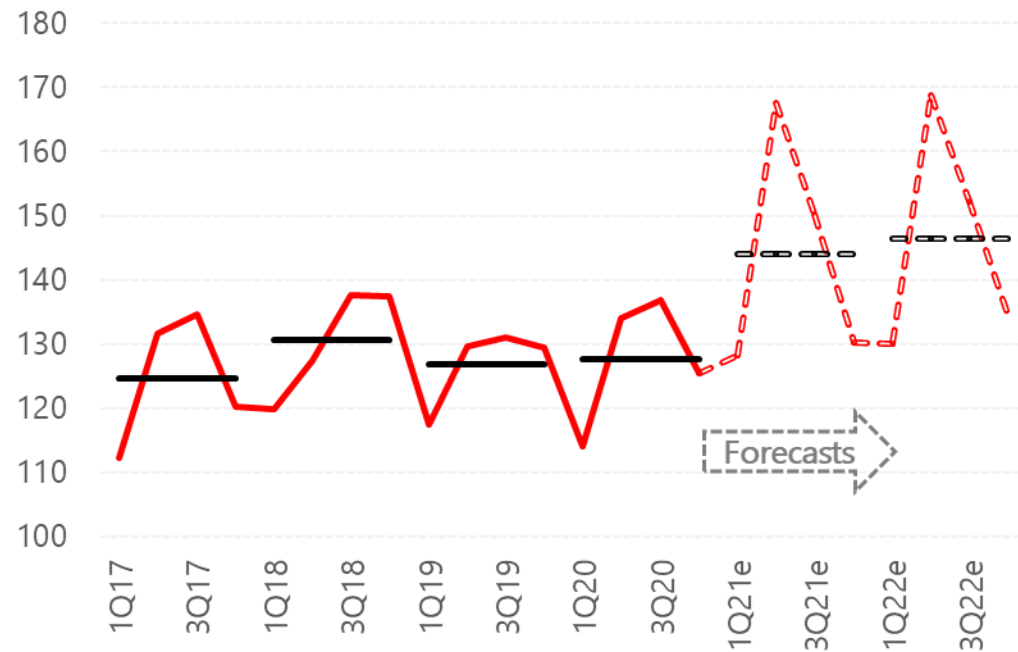


Sources: FUNCEX, Santander.

THE RABBIT AND THE TURTLE

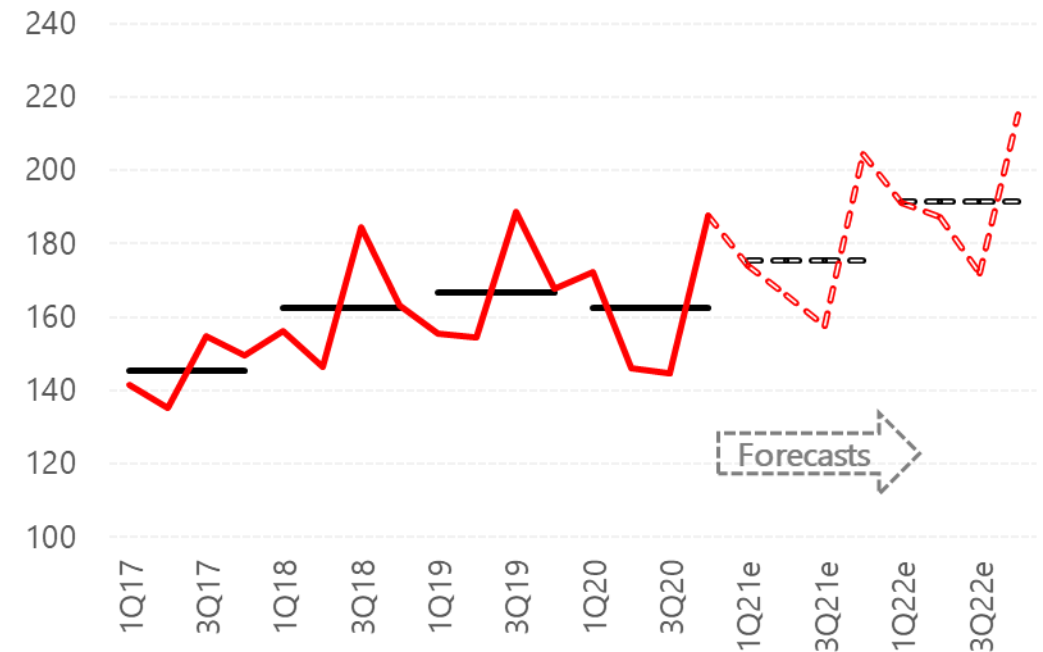
- While the lagged effects of the BRL weakening and the strong demand for commodities are likely to favor exports this year, we expect little additional improvement in 2022. On the import side, the gradual economic recovery should translate into a slow, but steady expansion in 2021 and 2022.

Export volume index (2006=100)



Sources: FUNCEX, Santander .

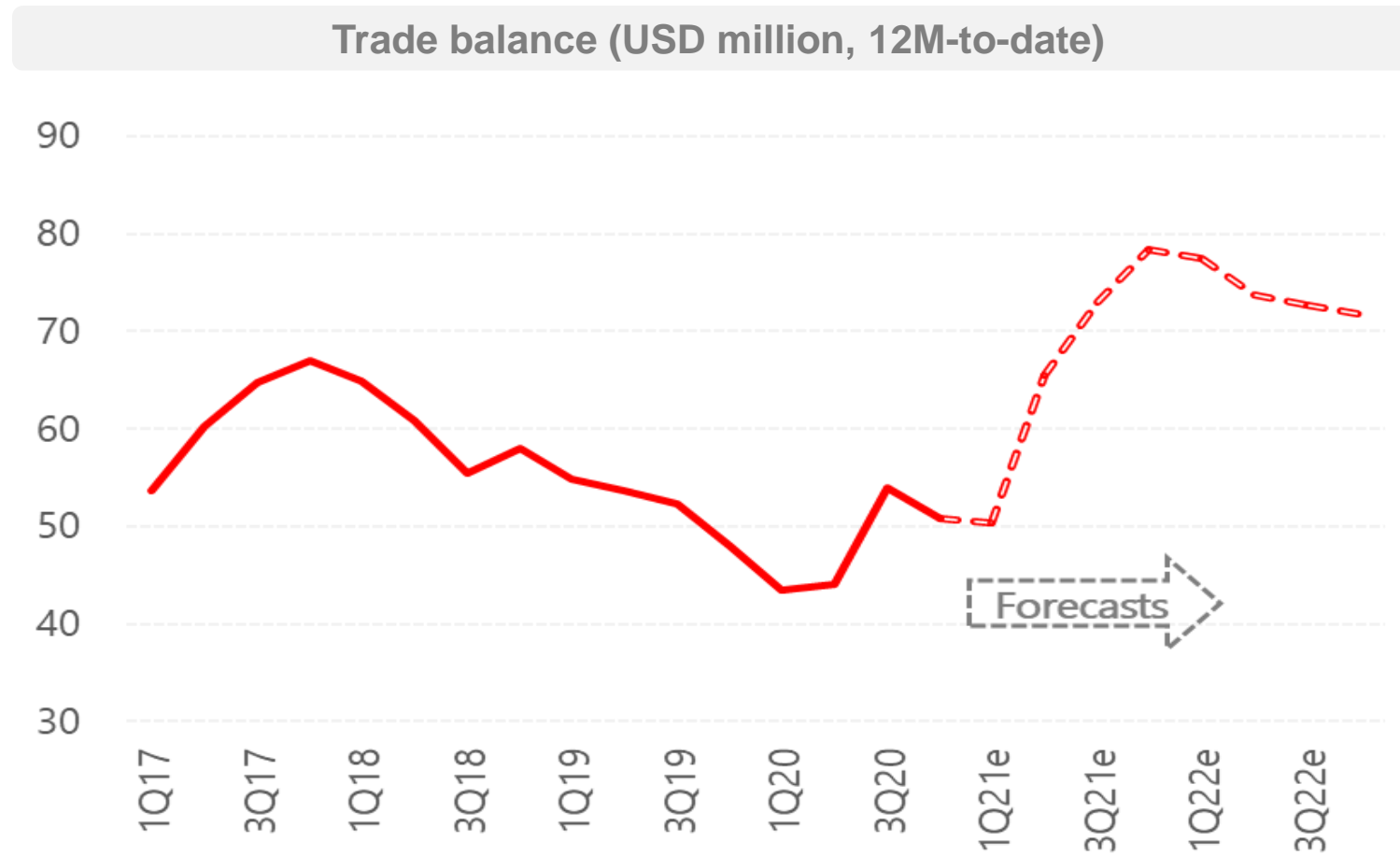
Import volume index (2006=100)



Sources: FUNCEX, Santander.

CHANGING TO A NEW LEVEL

- The combination of a weak currency in real terms, favorable commodity prices, growing trade flows, increasing demand for soft and metal commodities and a gradual economic recovery in Brazil should help the trade balance to register sizeable surpluses in the near future.

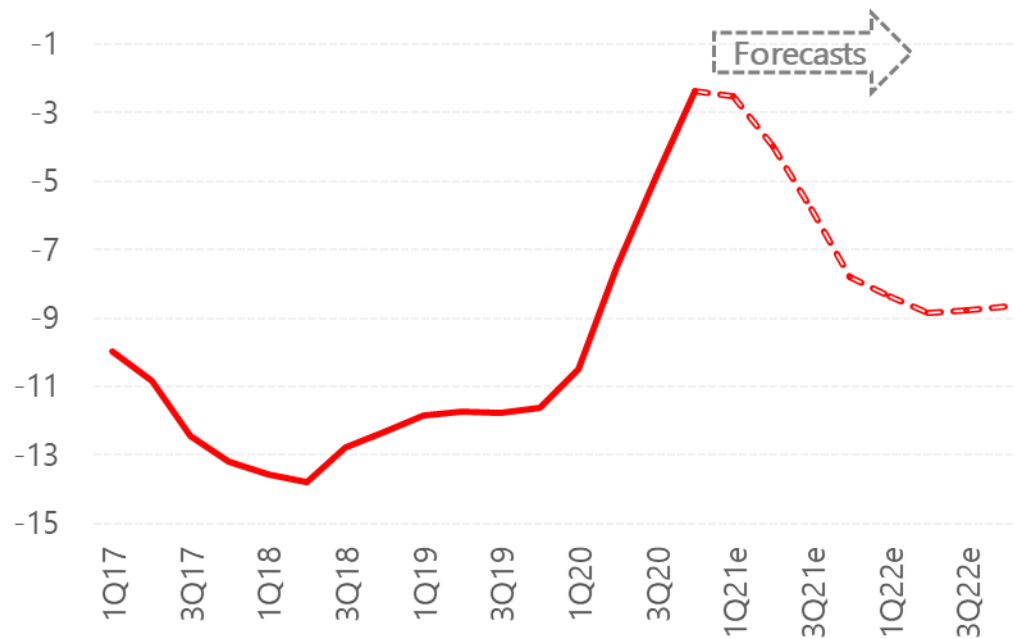


Sources: Brazilian Central Bank, Santander.

FASTER PACE, HIGHER SPENDING, BUT STILL FAR FROM “NORMAL”

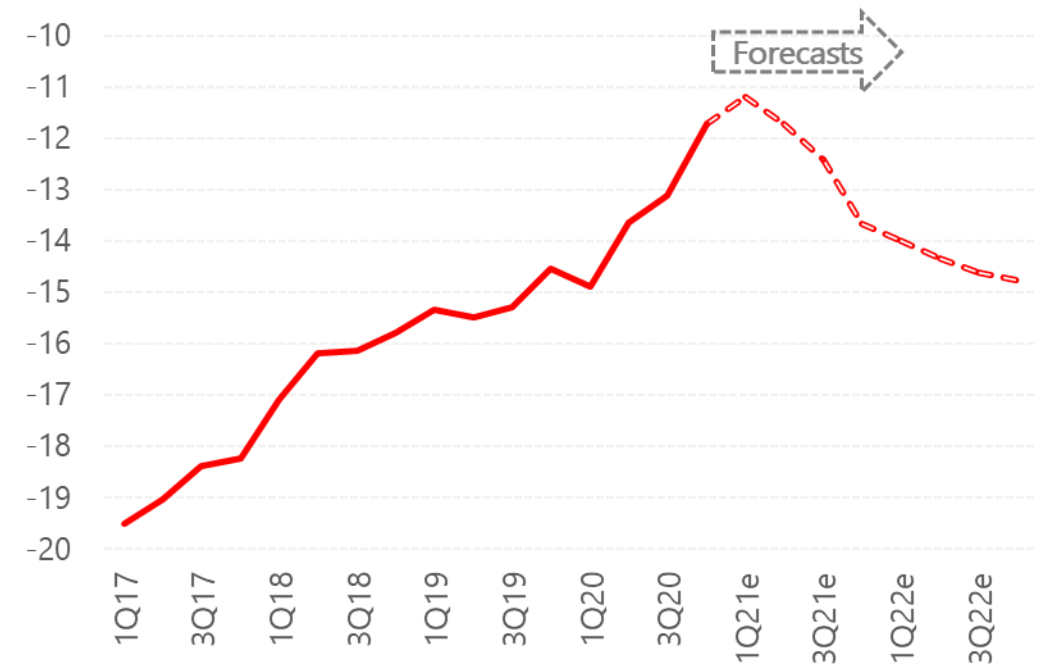
- Distension of mobility restrictions derived from the progress in the immunization against the Covid-19 and the increase in investments on the oil sector should lead to larger tourism outlays and equipment rental payments, although at a gradual pace.

Tourism net balance (USD million, 12M-to-date)



Sources: Brazilian Central Bank, Santander.

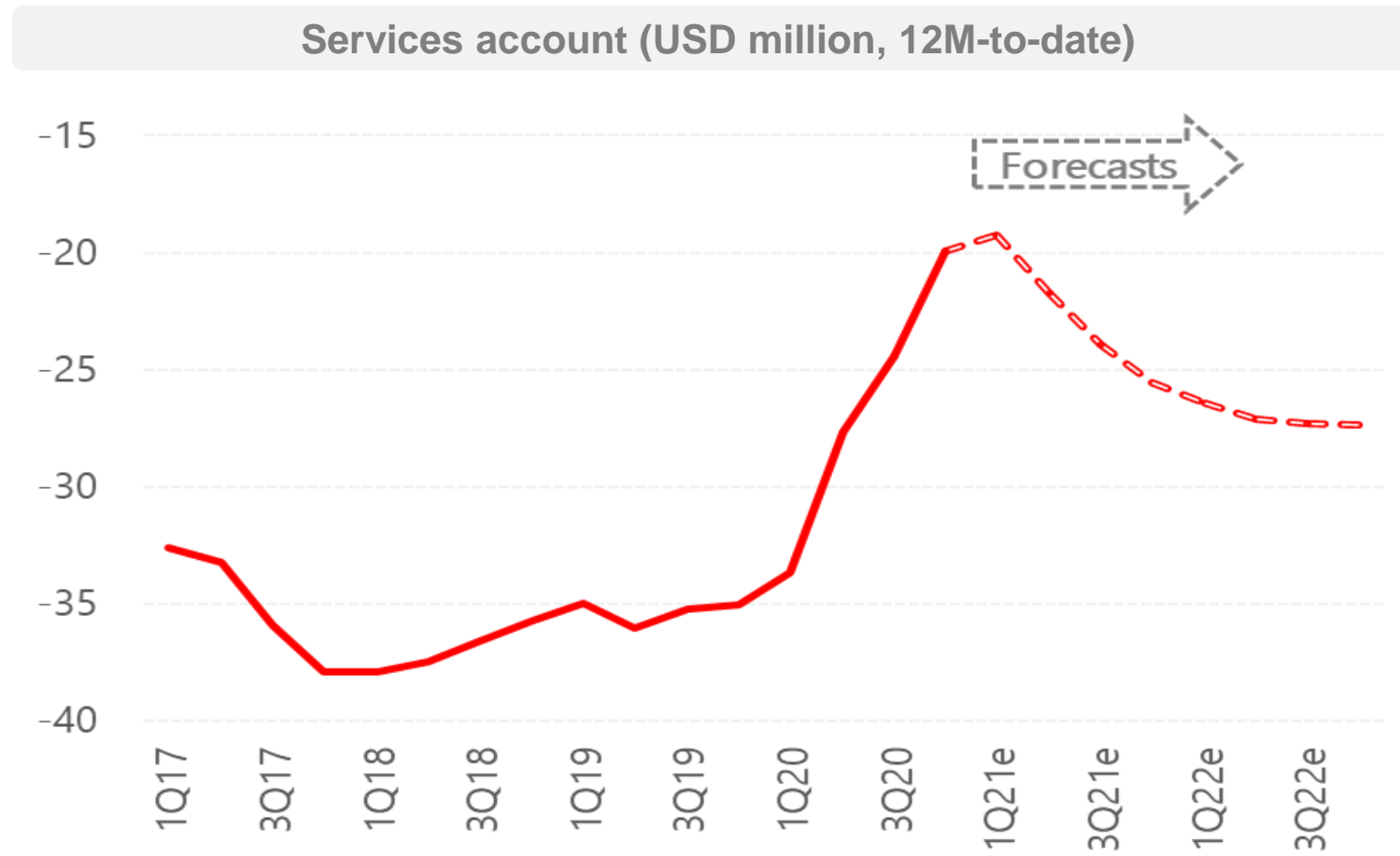
Equip. Rental (USD million, 12M-to-date)



Sources: Brazilian Central Bank, Santander.

A SLOW RETURN

- Services account should gradually become more negative as the economy gets back to normal.

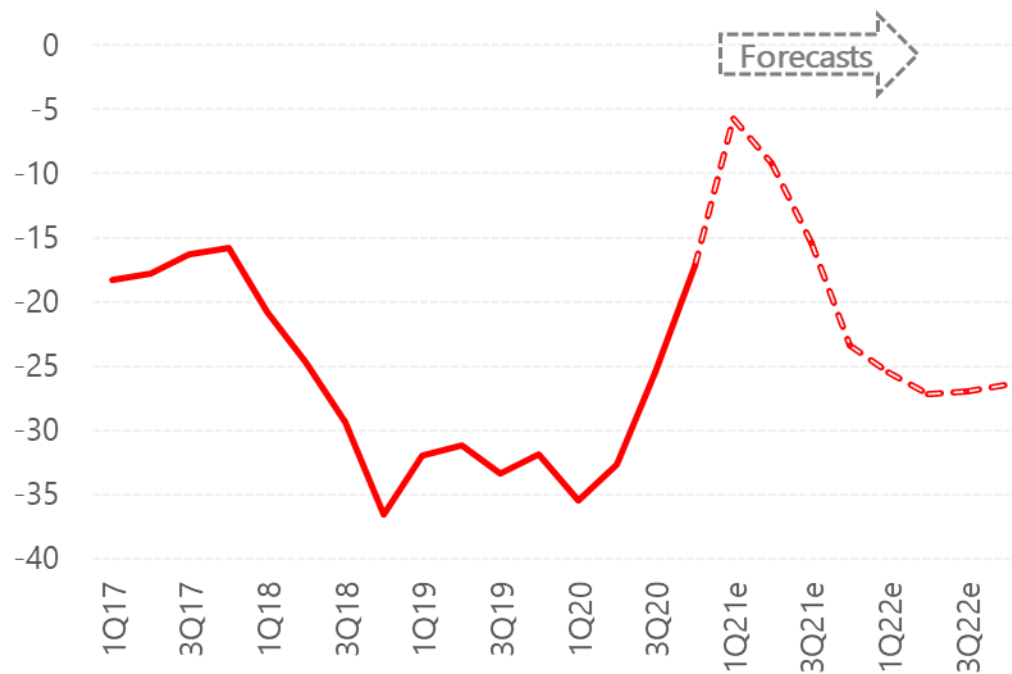


Sources: Brazilian Central Bank, Santander.

PARTNERS RATHER THAN CREDITORS

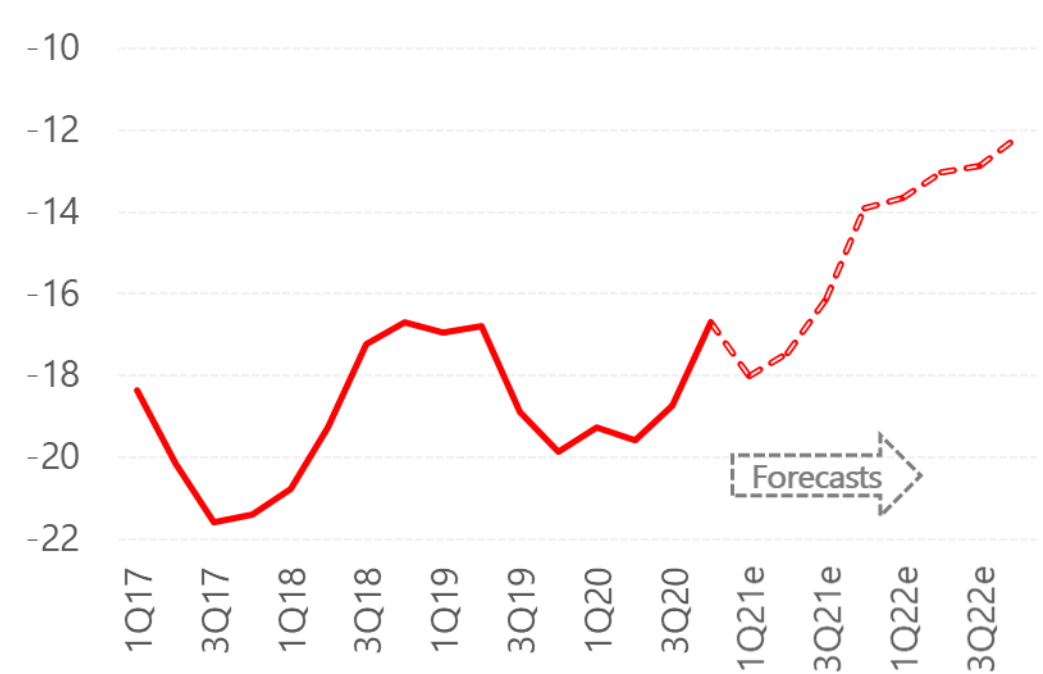
- The (expected) larger remittances of profits and dividends should be offset by the decline in the volume of external debt service, as the Brazilian corporate sector has improved its capital structure.

Profits & Dividends (USD million, 12M-to-date)



Sources: Brazilian Central Bank, Santander.

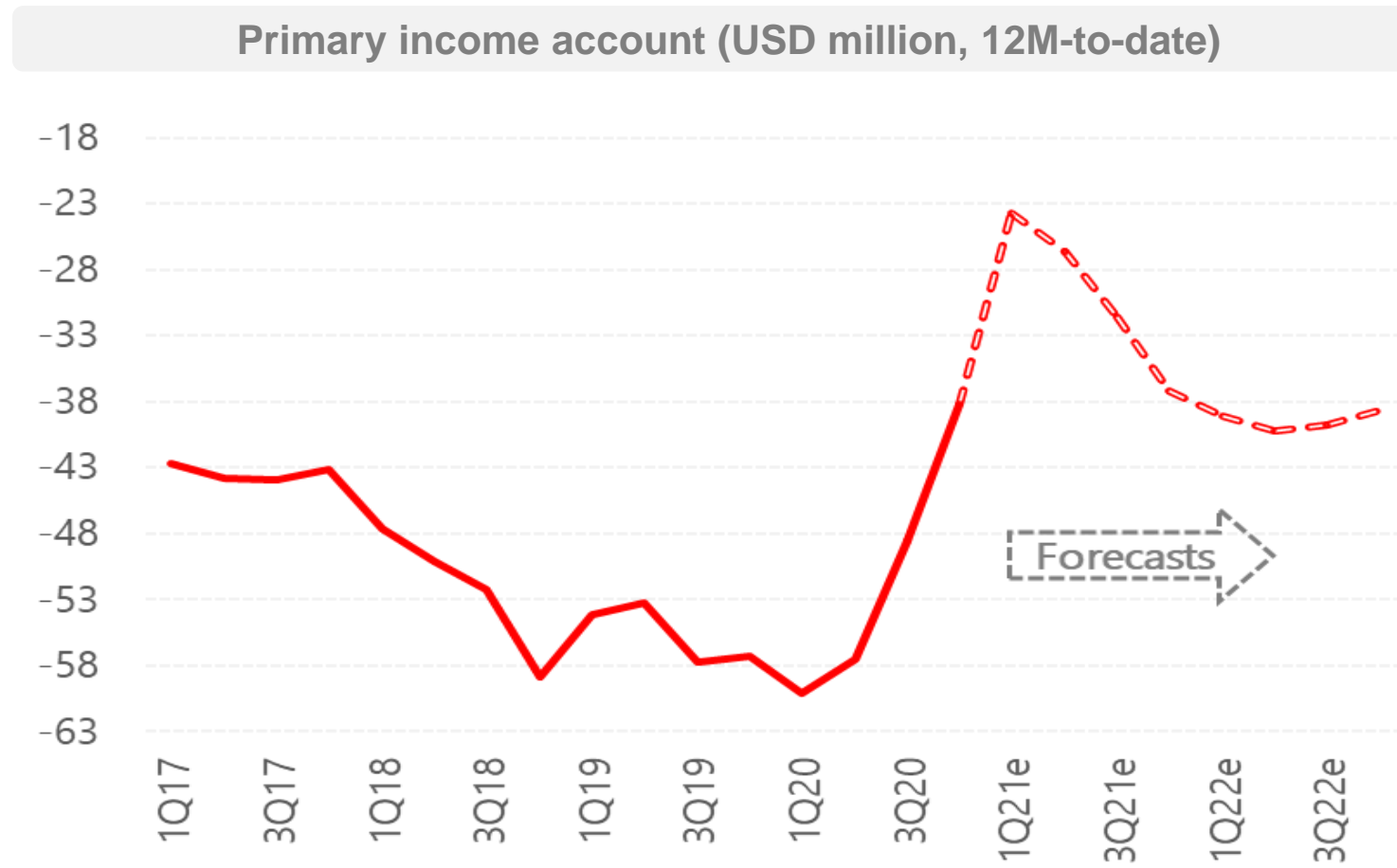
Interest payments (USD million, 12M-to-date)



Sources: Brazilian Central Bank, Santander.

PRO-CYCLICAL DYNAMICS, BUT WITH LIMITATIONS

- The gradual economic recovery should lead to a soft deterioration in the primary income account, which is likely to stabilize at much more comfortable levels than in the recent past.

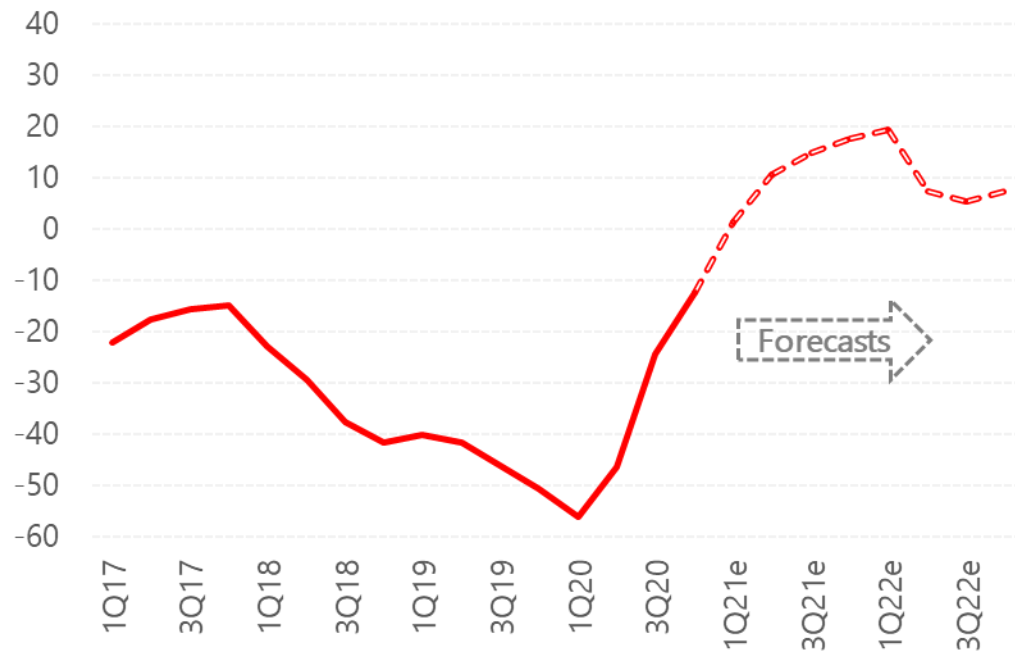


Sources: Brazilian Central Bank, Santander.

HEADING TOWARDS (UNUSUAL) SURPLUSES

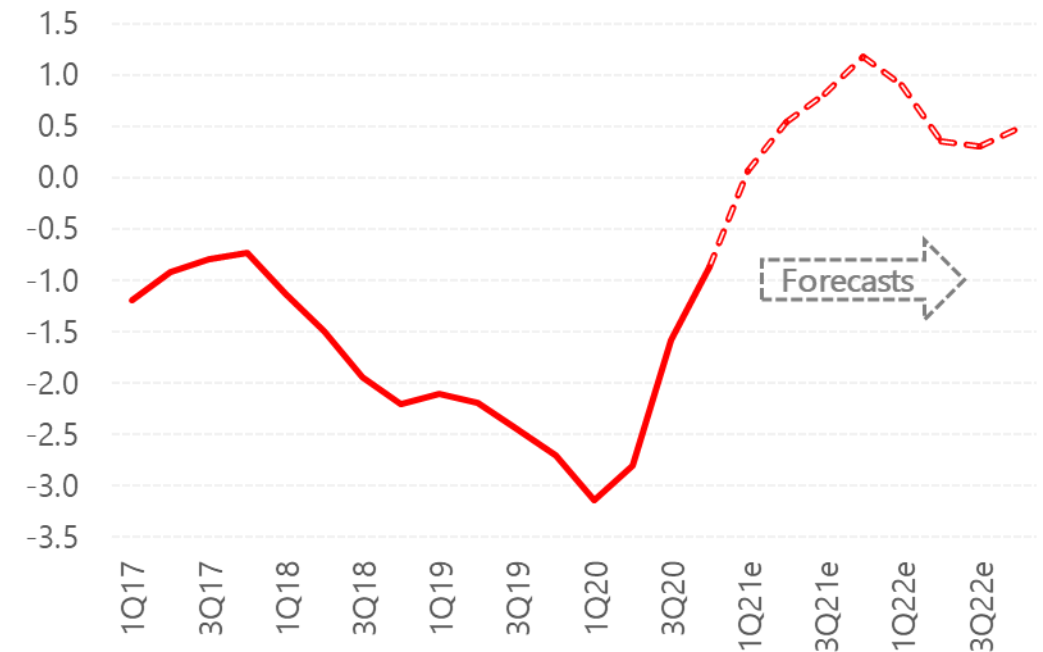
- We expect the adjustment in the current account balance to be continue, thus leaving it to register (unusual) surpluses on both this year and the next one.

Curr. Account Balance (USD million, 12M-to-date)



Sources: Brazilian Central Bank, Santander.

Current Account Balance (% of GDP)

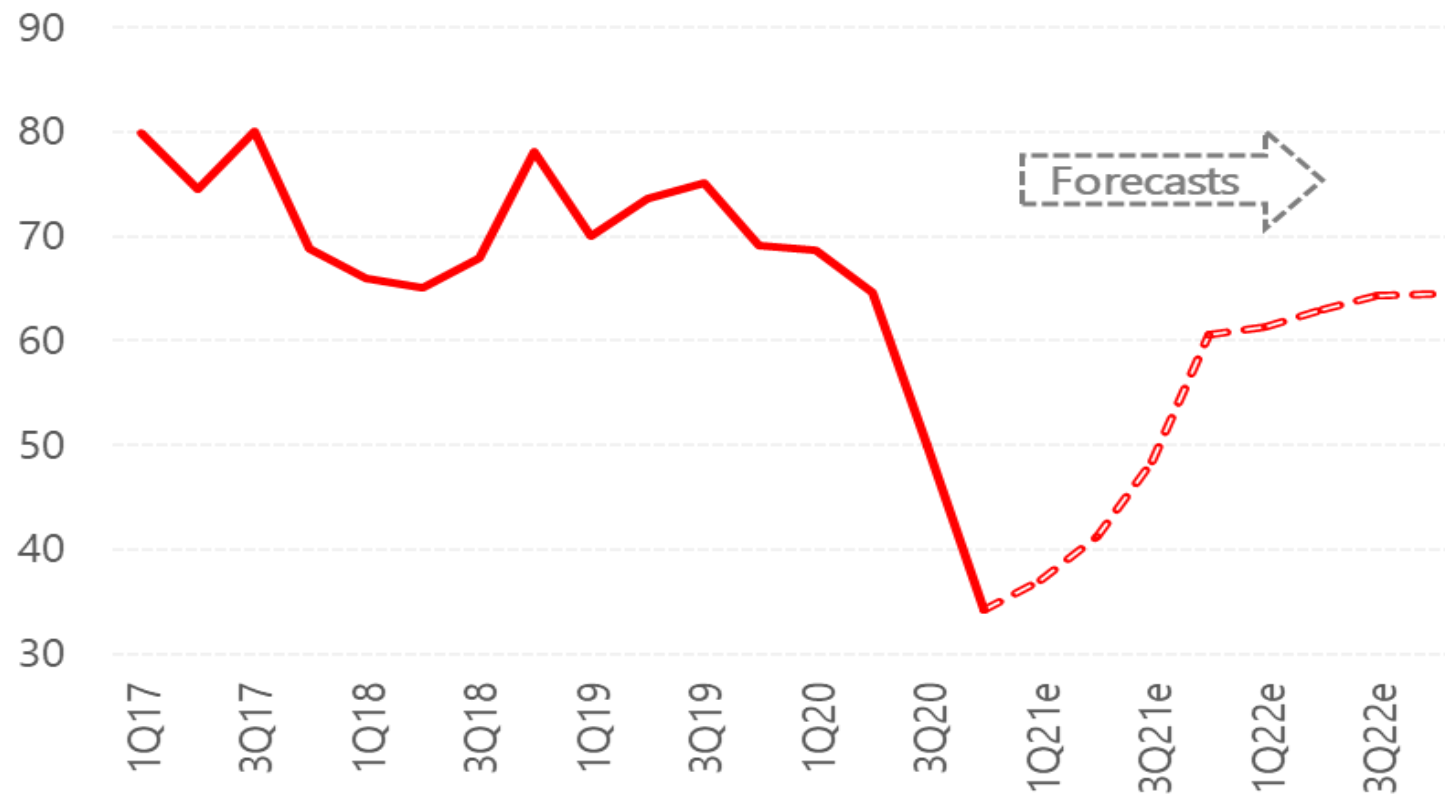


Sources: Brazilian Central Bank, Santander.

STEP BY STEP

- As the reformist agenda moves forward and the maintenance of the current fiscal framework becomes a reality, investors' confidence should increase and, consequently, direct investments in the country should expand.

Direct investment in the country (USD million, 12M-to-date)

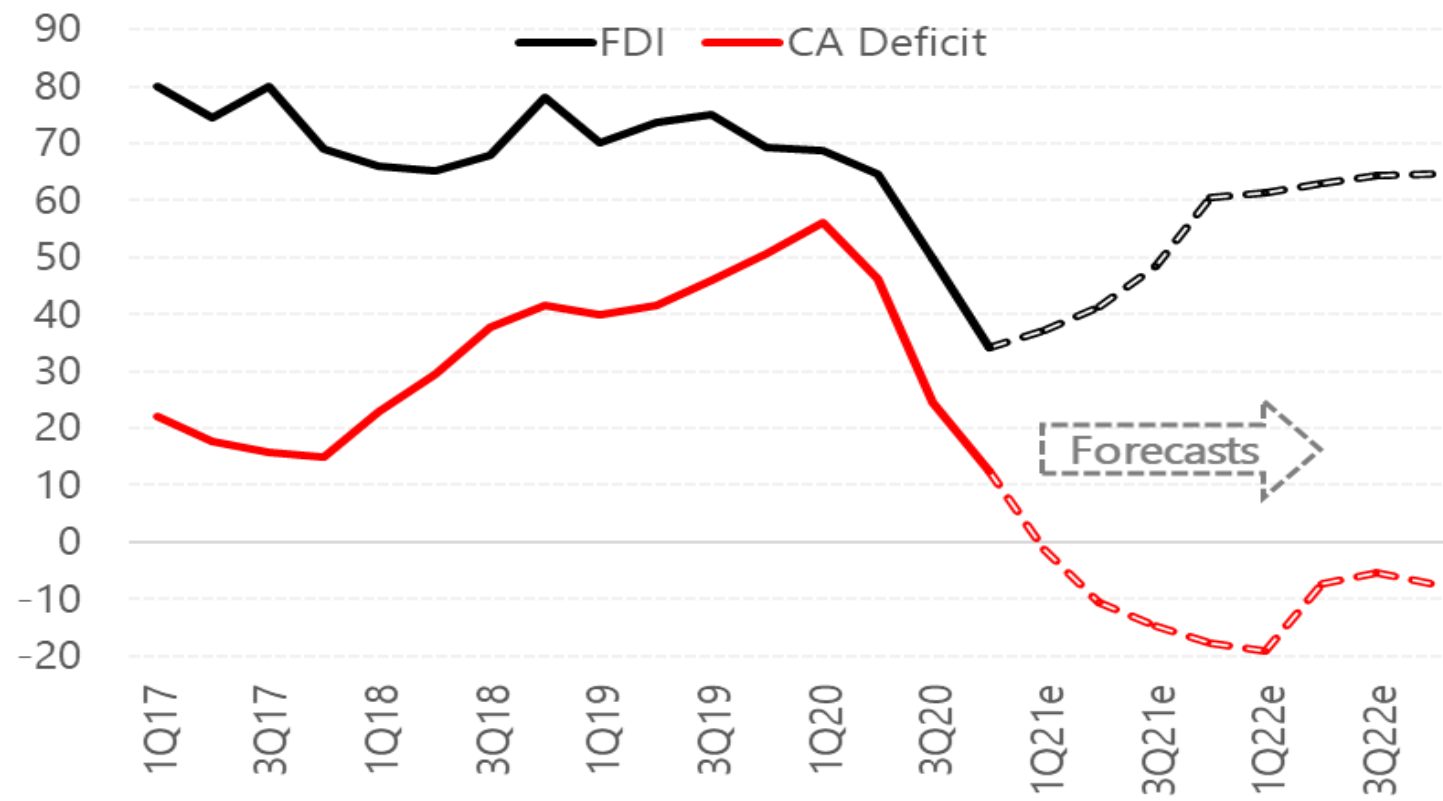


Sources: Brazilian Central Bank, Santander.

A (QUITE) COMFORTABLE SITUATION

- On the back of current account surpluses and the return of direct investments in the country, the Brazilian external financing needs should keep external sector data off market participants' radar for more than a while.

Dynamics of External Financing Needs (USD million, 12M-to-date)



Sources: Brazilian Central Bank ,Santander.

SOLID FUNDAMENTAL

- Based upon these indications, we maintain our view that the pressure on the FX rate has to do with elements other than external sector fundamentals.

Brazilian External Financing Needs				
USD billion	2019	2020	2021e	2022e
Current account balance	-50.7	-12.5	17.6	7.3
Trade balance	40.5	43.2	78.4	71.8
Exports	225.8	210.7	253.1	266.7
Imports	185.3	167.4	174.7	194.9
Services	-35.1	-19.9	-25.5	-27.3
Tourism	-11.6	-2.3	-7.8	-8.7
Eq. Rental	-14.6	-11.7	-13.7	-14.8
Others	-8.9	-5.9	-4.1	-3.9
Income	-57.3	-38.2	-37.2	-38.6
Profits & Dividends	-31.9	-17.2	-23.3	-26.5
Interest payments	-19.9	-16.7	-13.9	-12.2
Transfers	1.2	2.4	2.0	1.5
Direct investment onshore	69.2	34.2	60.6	63.8
External funding (-ve=shortage / +ve=excess)	18.5	21.6	78.2	71.1

Sources: Brazilian Central Bank, Santander.

Macroeconomic
forecasts

04

FORECASTS

Macroeconomic variables		Previous		Current
GDP (%)	2021E	2.9	↑	3.0
	2022E	2.3	↓	2.0
	2023E	1.8	→	1.8
IPCA (%)	2021E	3.6	↑	5.0
	2022E	3.2	↑	3.7
	2023E	3.3	→	3.3
Selic Rate (% end of period)	2021E	4.00	↑	5.50
	2022E	4.50	↑	6.00
	2023E	6.00	↑	7.00
FX Rate - USDBRL (end of period)	2021E	5.20	↑	5.25
	2022E	5.40	↑	5.55
	2023E	5.20	→	5.20
Current Account Balance (% of GDP)	2021E	1.2	→	1.2
	2022E	0.5	→	0.5
	2023E	-0.2	→	-0.2
Primary Fiscal Balance (% of GDP)	2021E	-3.1	↓	-3.2
	2022E	-2.2	→	-2.2
	2023E	-1.5	↓	-1.7
Gross Public Debt (% of GDP)	2021E	89.1	↓	86.2
	2022E	91.2	↓	88.8
	2023E	92.4	↓	91.2

Sources: Brazilian Central Bank, IBGE, Santander.

PARAMETERS

Selected Indicators				
Indicator	2020	2021e	2022e	
USDBRL	5.20	5.25	5.55	
DXY (1973=100)	89.9	92.0	95.0	
VIX (% pa)	22.8	15.0	15.0	
CRB Index (1967=100)	443.8	519.6	503.4	
Brazil 5Y CDS spread (bps)	142.9	300.0	325.0	
Interest rate differential (% pa)	1.75	5.25	5.75	
CPB Index (2010=100, sa)	124.1	128.6	129.7	
Brazilian REER (Jan02=100)	210.9	199.8	210.9	

Sources: Bloomberg, Santander.

Contacts

05

Thank you.

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Our culture is based on believing that everything we do should be:

Simple Personal Fair



Raissa Freitas
Business Manager
raifreitas@santander.com.br
+55 (11) 3553-7424

Brazil Macroeconomic Research Team

Ana Paula Vescovi
Chief Economist
anavescovi@santander.com.br
+55 (11) 3553-8567

Jankiel Santos
Economist – External Sector
jankiel.santos@santander.com.br
+55 (11) 3012-5726

Tomas Urani
Economist – Global Economics
tomas.urani@santander.com.br
+55 (11) 3553-9520

Lucas Maynard
Economist – Economic Activity
lucas.maynard.da.silva@santander.com.br
+55 (11) 3553-7495

Gilmar Lima
Economist – Modeling
gilmar.lima@santander.com.br
+55 (11) 3553-6327

Mauricio Oreng
Head of Research & Strategy
mauricio.oreng@santander.com.br
+55 (11) 3553-5404

Ítalo Franca
Economist – Fiscal Policy
italo.franca@santander.com.br
+55 (11) 3553-5235

Daniel Karp Vasquez
Economist - Inflation
daniel.karp@santander.com.br
+55 (11) 3553-9828

Felipe Kotinda
Economist - Credit
felipe.kotinda@santander.com.br
+55 (11) 3553-8071

Gabriel Couto
Economist – Special Projects
gabriel.couto@santander.com.br
+55 (11) 3553-8487

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