



## CORE INFLATION TREND NEARS DOUBLE-DIGIT TERRITORY

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- In the rolling week ended on February 17, the USD/BRL pair closed the period at 5.17 (a 1.5% gain) and stood out as the top performer in the basket with the 31 most liquid currencies in the world. In our view, the move was mostly related to the continuation of the recent global asset reallocation trend and the maintenance of constructive market assumptions about economic policy ahead.
- The local yield curve flattened further in recent days, reflecting some selling in the front end (on persistent inflation jitters) and a lack of direction in the back end. The inversion in the 2s/5s segment turned even more pronounced.
- The IBC-Br (BCB's monthly GDP proxy) jumped 0.33% MoM-sa in December, the second gain in a row. December's result follows widespread growth seen among the main sectors in the period, and places the index 0.3% above the pre-pandemic mark (February 2020). The BCB announced a significant upward revision in the historical series. Our 4Q21 GDP growth tracking stands at +0.4% QoQ-sa, consistent with a full-2021 reading of 4.6%, and generating a 0.1% carryover for 2022. We forecast 0.7% GDP growth this year.
- In the coming week, FGV will release the first batch of economic confidence data for February: the economic confidence indexes for consumers and industry are due out on Tuesday (February 22) and Thursday (February 24), respectively, while the tertiary sector data are due out on Friday (February 25). On Thursday (February 24), IBGE will publish the December PNAD household survey: we estimate the unemployment rate at 11.3% nsa, equivalent to 12.0% sa according to our own seasonal adjustment (November: 12.1%).
- We expect February's IPCA-15 (due on Wednesday, February 23) to rise 0.87% MoM. In YoY terms, this means +10.64%, faster than January's IPCA-15 (10.20%), reinforcing our expectation of a plateau in annual inflation until April 2022. In terms of underlying inflation measures, we estimate the EX3 core (services and industrials) will be trending close to 10% 3MMA-saar, way above the upper target (5%). Despite a much tighter monetary policy, we continue to see headwinds facing the disinflation process ahead, and we forecast an above-consensus 6.0% IPCA for 2022 (consensus: 5.5%).

***Most of the information in this report is up to the end of Thursday, February 17, 2022.***

**IMPORTANT DISCLOSURES/CERTIFICATIONS ARE IN THE "IMPORTANT DISCLOSURES" SECTION OF THIS REPORT.**

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**Figure 1. Brazil Macro Agenda for the Week of February 20 to February 26, 2022**

Indicators / Events	Source	Reference	Date	Santander Estimate	Prior
Consumer Confidence (index)	FGV	Feb/22	Tue, 22-Feb	-	74.1
Construction Confidence (index)	FGV	Feb/22	Wed, 23-Feb	--	92.8
<b>IPCA-15 Inflation (% MoM)</b>	<b>IBGE</b>	<b>Feb/22</b>	<b>Wed, 23-Feb</b>	<b>0.87</b>	<b>0.58</b>
IPCA-15 Inflation (% YoY)	IBGE	Feb/22	Wed, 23-Feb	10.6	10.2
Current Account Balance (USD billion)	BCB	Jan/22	Wed, 23-Feb	-7.0	-5.9
Foreign Direct Investment (USD billion)	BCB	Jan/22	Wed, 23-Feb	3.5	-3.9
Federal Debt Report (BRL trillion)	STN	Jan/22	Wed, 23-Feb	-	-6.7
National Unemployment Rate (% nsa)	IBGE	Dec/21	Thu, 24-Feb	11.3	11.6
<b>National Unemployment Rate (% sa)</b>	<b>IBGE</b>	<b>Dec/21</b>	<b>Thu, 24-Feb</b>	<b>12.0</b>	<b>12.1</b>
Industrial Confidence (index)	FGV	Feb/22	Thu, 24-Feb	-	98.8
Total Outstanding Loans	BCB	Jan/22	Thu, 24-Feb	-	468
Central Gov. Prim. Balance (BRL billion)	STN	Jan/22	Thu, 24-Feb	68.5	13.8
Primary Budget Balance (BRL billion)	BCB	Jan/22	Fri, 25-Feb	81.2	0.1
Retail Confidence (index)	FGV	Feb/22	Fri, 25-Feb	-	84.9
Services Confidence (Index)	FGV	Feb/22	Fri, 25-Feb	-	91.2
Federal Tax Collection (BRL billion)	RFB	Jan/22	22 to 26-Feb	232.9	193.9

Sources: Bloomberg, IBGE, Santander.

**For details on Santander's economic forecasts for Brazil, please refer to our last Scenario Update<sup>1</sup>.**

**Also refer to our Macro Propositions for Brazil in 2022<sup>2</sup>.**

<sup>1</sup> Santander Brazil – Scenario Update: “Inflation Still a Concern” – January 20, 2022- Available on: <https://bit.ly/Std-scenupdate-jan22>

<sup>2</sup> Santander Brazil – Macro Propositions 2022: “Navigating the Uncertainties” – January 07, 2022- Available on: <https://bit.ly/Std-Macroprop22>



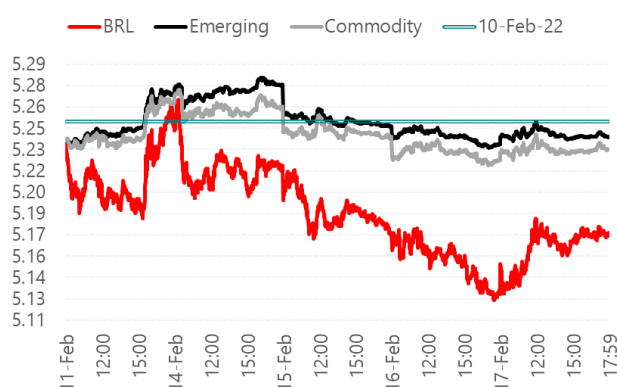
## LOCAL MARKETS—FX

In the rolling week ended on February 17, the USD/BRL pair closed the period at 5.17 (a 1.5% gain) and stood out as the top performer in the basket with the 31 most liquid currencies in the world. In our view, the move was mostly related to the continuation of the recent global asset reallocation trend and the maintenance of constructive market assumptions about economic policy ahead. Given the lack of economic releases, the domestic news cycle was fairly muted and does not seem to have had a major influence on the local FX market in recent days. In our view, the international news cycle did not show a clear influence on local markets either. For example, while on the one hand, the continuing tensions involving Russia and Ukraine may have contributed to reduce slightly the global risk appetite, the less hawkish tone of the Fed's FOMC minutes lent a little help to risky currencies in general. All in all, we do not identify a clear predominant driver behind the Brazilian currency in the very recent days, but we recognize that the (tactical) momentum continues. We continue to expect some weakening of the BRL in the coming months, given the uncertainties related to economic policy from 2023 onward.

## LOCAL MARKETS—Rates

The local yield curve flattened further in recent days, reflecting some selling in the front end and a lack of direction in the back end. The inversion in the 2s/5s segment turned even more pronounced. Since Thursday (February 11), the front end of the curve (Jan-24 DI future) rose 18 bps to 12.02%, while the back end of the curve (Jan-27 DI future) rose 3 bps to 11.33%. At the same time, the curve's steepness in this segment decreased further by 15 bps to -69 bps, making the inversion even more pronounced in this segment. At the front end, there was no specific news, but the continuing buoyancy in commodity prices in USD (despite the appreciation of the BRL) and the surprises in international inflation numbers (U.S. PPI, for example) may have influenced the rise of short yields. We remind readers that the BCB estimates that nearly 70% of the excess inflation last year (vis-à-vis the mid-target) was due to imported inflation. Both the curve itself and the options market keep pricing in a 100-bp hike in the Selic at the next Copom meeting as the most likely scenario (in line with our forecast). At the back end, the absence of relevant news on the domestic fiscal front, along with the lack of a clear trend for the 10-year U.S. Treasury yield during the last few days apparently prompted domestic long-end yields to move sideways. Fundamentally speaking, we continue to see an environment of high uncertainties for the domestic economy, particularly regarding the fiscal consolidation process, and we continue to see room for domestic yields to re-steepen after both IPCA inflation and the Selic rate see a peak.

Figure 2. USD/BRL Intraday Trends

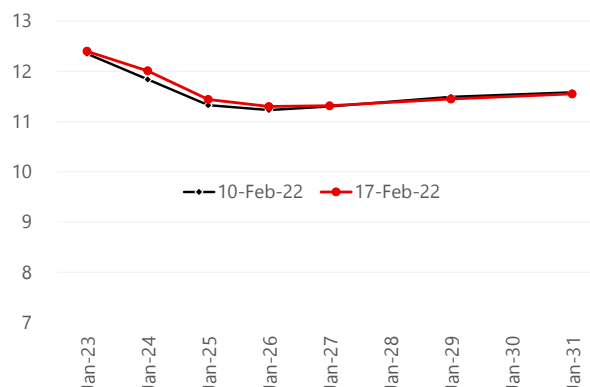


Sources: Bloomberg, Santander.

Note 1: As of the close on Thursday, February 17, 2022.

Note 2: For other currencies, we use USDBRL values as a base-index.

Figure 3. Brazilian Domestic Yield Curve (% p.a.)



Sources: Bloomberg, Santander.

Note: As of the close Thursday, February 17, 2022.



## COMMODITIES

**Commodities prices retreated this week.** The Bloomberg Commodity Aggregate Index in BRL receded 0.3% in the rolling week ended February 17. In USD terms, the index rose 1.9%. The Agriculture Subindex rose 0.9% and the Energy Subindex gained 3.6%, whereas the Industrial Metals Subindex receded -1.0%. In our view, idiosyncratic factors (such as adverse weather, low inventories, and rising costs of production) continue to feed the commodity rally early in 2022.

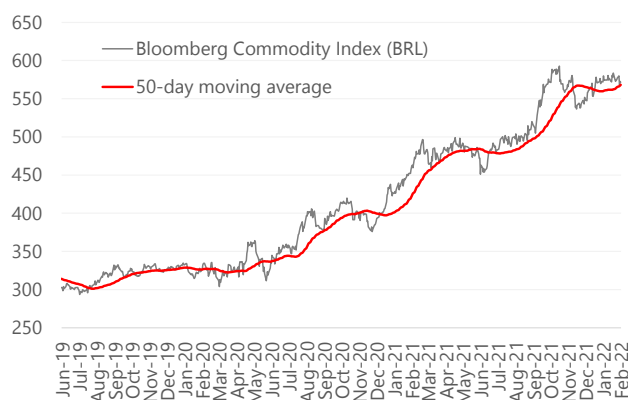
**U.S. soybean exports rising at a time of year when Brazilian shipments typically dominate.** As prospects for South American crops continue to deteriorate, importers have been turning to American soybeans as the premium paid for Brazil's cargoes soars. Importantly, the short-term weather outlook is still mostly dry for South Brazil and Argentina. With high soybean prices, we think U.S. farmers will likely be encouraged to increase their planted area. Furthermore, the price of soybean oil rose 3.3% in the week (reaching the highest level since May 2021) following a fire at a top U.S. biodiesel plant.

**Brent oil retreats after reaching \$94/bbl as Iran nuclear talks progress.** While the Russia-Ukraine crisis continues, U.S.-Iran negotiations are getting closer to an agreement, according to press sources<sup>3</sup>, which could potentially mean additional barrels in the market. EIA reported on Wednesday (February 16) a steeper decline in U.S. crude stockpiles, though inventories are close to the lowest level since October 2018. We still see output shortages in the oil market, as global inventories are low, and producers (ranging from OPEC+ members to independent U.S. shale companies) struggle to boost supply following the underinvestment in recent years.

**Iron ore slumps 7% as Chinese crackdown steps up.** Following the iron ore rally early this year, mirroring expectations that demand will pick up this year, big trading companies were due to meet with Chinese government officials to discuss "abnormal" prices. Other Chinese government measures to counter the iron ore rally include port checks, higher futures trading fees, and a pledge to crack down on speculation, with companies being asked to provide detailed information on recent inventory changes.

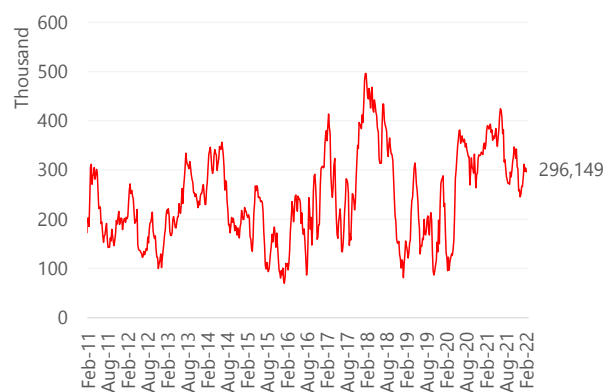
**CFTC<sup>4</sup> reports a decrease in speculative long positions in WTI crude oil.** Money managers reduced their net long WTI crude futures and options positions in the week ended February 8, the CFTC reported last Friday (February 11). The positions in futures and options decreased by 7,723 contracts to 296,149.

**Figure 4. Bloomberg Commodity Index in BRL**



Sources: CBOT, Santander.

**Figure 5. CFTC NYMEX Crude Oil Managed Money Net Total (Number of contracts)**



Sources: COT, Santander.

<sup>3</sup> <https://www.reuters.com/world/middle-east/decision-iran-nuclear-deal-days-away-ball-tehrans-court-france-2022-02-16/>

<sup>4</sup> U.S. Commodity Futures Trading Commission.

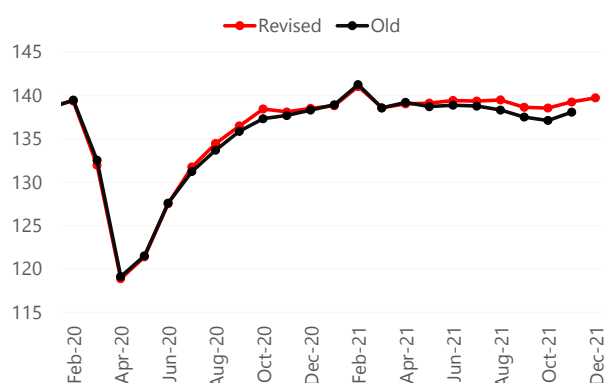


## ECONOMIC ACTIVITY

**Broad activity continued to strengthen in December.** The IBC-Br jumped 0.33% MoM-sa (+1.30% YoY) in December, with the series being revised upward considerably. December's figure places the economy 0.3% above the pre-pandemic mark (February 2020), according to this indicator, with broad activity reaching the highest reading since the recent spike seen in February 2021 (down 0.9% since this mark). Among key sectors, December's result summarizes the widespread growth seen in the period, with a slight increase in broad retail sales (+0.3% MoM-sa), and with strong growth in industrial output (+2.9% MoM-sa) and services' real revenue (+1.4% MoM-sa). We also recognize that farm output's rebound (after the sharp drop seen in 3Q21) and the continued recovery of health and education services (not captured in the monthly surveys) may have contributed positively as well. Our 4Q21 GDP growth tracking stands at +0.4% QoQ-sa, consistent with 4.6% GDP growth in 2021 and generating a 0.1% carryover for 2022. We forecast 0.7% growth this year. [See details in the link<sup>5</sup>.](#)

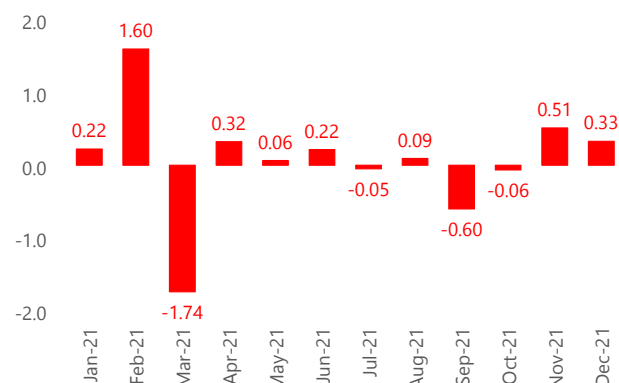
**In the coming week, FGV will release the first batch of economic confidence data for February.** The economic confidences indexes for consumer and industry are due out on Tuesday (February 22) and Thursday (February 24), respectively, while the tertiary sector data are due out on Friday (February 25). Moreover, on Thursday (February 24), the December PNAD household survey is due to be released. We estimate the unemployment rate at 11.3%, equivalent to 12.0% in our seasonally adjusted figure (November: 12.1%). The following weeks will have a different schedule than usual for labor market indicators. The January CAGED survey is expected to be released by the Ministry of Labor only on March 10. Furthermore, the IBGE plans to correct the one-month lag of the PNAD survey (in place since the beginning of the pandemic) with two data-point releases in March. The January survey is expected on March 18, and the February survey is due to be released on March 31. [For details on Santander's activity outlook, please refer to our last chartbook<sup>6</sup>.](#)

Figure 6. IBC-Br (sa, 2003=100)



Sources: BCB, Santander.

Figure 7. IBC-Br (sa, MoM %)



Sources: BCB, Santander.

<sup>5</sup> Santander Brazil Economic Activity: "Broad Activity Continued to Strengthen in December" – February 11, 2022 – Available on: <https://bit.ly/Std-econact-021122>

<sup>6</sup> Santander Brazil Economic Activity: "Chartbook – Maintaining the Main Growth Drivers for 2022" – February 01, 2021 – Available on: <https://bit.ly/Std-chart-econact-feb22>



## INFLATION

**We expect February's IPCA-15 (due on Wednesday, February 23) to rise 0.87% MoM. In YoY terms, this means +10.64%, faster than January's IPCA-15 (10.20%), reinforcing our expectation of a plateau in annual inflation until April 2022.** In terms of headline trends—as measured by the seasonally adjusted and annualized three-month moving average—we expect some softening to 5.3% 3MMA-saar, compared to a prior reading of 8.2% and a peak of 12.3% in November 2021.

Compared to January's IPCA-15 (+0.58% MoM), we expect the headline to accelerate in monthly terms, driven mostly by free-market prices (+1.18% MoM vs. +0.92% last month). Particularly, we believe services accelerated in monthly terms (1.39% MoM vs. 0.51 % previously), due to the seasonal annual adjustment of education fees that are almost fully accounted for in February. With this monthly result, we expect the services trend to accelerate to 7.0% 3MMA-saar (from 5.0%), and we forecast further acceleration at least until mid-year. We expect industrial goods to decelerate in monthly terms (+0.93% MoM vs. +1.46% previously), enough to keep the trend hovering around (a whopping) 14.0%. Finally, we estimate food-at-home remained almost stable at 1.08% MoM, with the trend accelerating to 6.7%.

In terms of broad underlying inflation measures, we estimate the EX3 core rose 0.87% MoM, which would represent a quickening trend to ~9.6% 3MMA-saar. If correct, January would be the 17th consecutive month in which the EX3 core has run above the BCB's mid-target in 3MMA-saar terms (our headline CPI target is 3.50% for 2022 and 3.25% for 2023). We remain cautious regarding the inflation outlook, especially after the recent rise in fiscal risks, which could push expectations even higher and make inertia even stronger, posing difficulties for the disinflation process ahead.

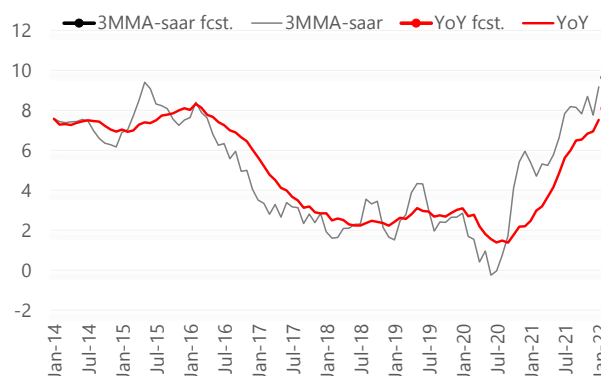
Despite a much tighter monetary policy, we continue to see challenges for the disinflation process ahead, and we forecast an above-consensus 6.0% IPCA for 2022 (consensus: 5.5%).

**Figure 8. February's IPCA-15 Details (%)**

	MoM		YoY	
	Santander	Contrib.	Jan-22	Feb-22
<b>IPCA</b>	<b>0.87</b>	<b>0.87</b>	<b>10.2</b>	<b>10.6</b>
Administered	0.06	0.02	16.6	16.4
Free	1.18	0.86	8.0	8.7
Food-at-home	1.08	0.16	8.5	9.0
Industrial goods	0.93	0.22	12.3	12.7
Services	1.39	0.48	5.1	6.0
<b>EX3 Core</b>	<b>0.87</b>	<b>0.31</b>	<b>7.5</b>	<b>8.1</b>

Sources: IBGE, Santander.

**Figure 9. Core Inflation EX3 (%)**



Sources: IBGE, Santander.



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