The impact of the Covid-19 pandemic will extend into the year 2021, in our view, causing mobility restrictions, a slower economic recovery, possible reintroduction of (moderate) stimuli, as well as social and political uneasiness.

Pandemic control is key to global activity recovery, in our opinion
Ability to vaccinate the population will dictate the pace of resumption.

Vaccines and China’s growth expected to support commodity markets
Optimism over global growth expected to prevail in 2021.

After a slow start, we expect Brazil’s Covid-19 vaccination campaign to gather momentum
Risks of vaccine delays should be limited to 1H21, in our view.

Important measures and reforms that could be implemented
Beyond the question of vaccination, we believe certain measures and reforms are necessary to support the reduction of idiosyncratic risks.

Fiscal accounts on a tightrope with the possible reintroduction of emergency aid
We now see the resumption of the emergency aid, in much smaller size, and partially offset by the approval of fiscal reforms.
Groundhog Year?
Santander Brazil’s Macro Propositions for 2021

Lingering (mobility and wage) impacts of the pandemic to slow the speed of recovery
After a weak start in 1Q21, we expect progress in vaccination and a rise in mobility to reignite economic activity from 2Q21 onwards.

Normalization in the labor force expected to lead to a higher unemployment rate
After the sharp drop in the size of the labor force in 2020, we expect a normalization process (more people searching for jobs) in 1H21.

Drop in “expanded” real wage bill, despite a new round of emergency aid
At much smaller size, the reintroduction of emergency aid will not avoid a steep decline in the “expanded” real wage bill vs. 2020.

Capital markets expected to support economic activity
Bank credit to companies should decelerate from 2020 levels, in our view, but capital markets have significant room for growth.

A benign inflation scenario, but with a risky path
We look for full-year inflation below the target, but with a (risky) landing in 2H21.

A less accommodative monetary policy stance in 2021 and 2022
The BCB is signaling increased discomfort about the “extraordinary” level of stimulus, with a Selic policy rate at 2.00%.

Spoiling the opportunity to fix the roof
We think the continuation of constructive global conditions should favor some BRL strengthening this year, but uncertainties remain.
Overview: propositions for 2021, in short

The central issue in 2021 will be vaccination, in our view. Just as the outbreak of the Covid-19 pandemic in 2020 exacerbated fiscal problems and the perception of inequalities in Brazil, we believe vaccination will be decisive both for the normalization of economic activity and for the definition of public policies. As a second wave of infections continue to unfold, and since it will take time for the vaccination process to gain traction, there will be additional mobility restrictions in the 1Q21 and, consequently, a GDP contraction in the period. We expect approximately 50% of the population to be immunized by the end of the year. The return to economic recovery mode after the removal of the strong fiscal stimulus of 2020 will be more noticeable in the 2H21, in our view, in the wake of a more intensive vaccination campaign. Before then, we believe there will be additional economic stimulus from the government, especially a new emergency aid package – temporary, for a smaller amount, and with less scope. In the first half of the year, we forecast that inflation accumulated in 12 months will reach its peak, with subsequent convergence toward the center of the target. We expect the monetary policy committee to start an early cycle of partial normalization of the Selic rate. We forecast that the BRL will follow its appreciation trend, driven by greater global growth, an improvement in global financial conditions, and a recovery in commodity prices. The appreciation, however, will be largely contained by the limited progress on macro reforms, the maintenance of fiscal risk, and the uncertainties in the political-institutional field, in our view. With the escalation of electoral disputes for speakers in Congress, we believe political frictions are likely to hinder the advances of reforms and anticipate the start of the 2022 electoral race. Thus, for the year 2021 we see risks still high, squeezed between the course of the pandemic and a premature start of the electoral race, in the absence of substantial reforms on one hand or substantial disruptions in the economic environment on the other.
Pandemic control is key to resumption of global activity, in our view

- Ability to vaccinate the population will dictate the pace of resumption, in our view:

   The coronavirus pandemic has brought an unprecedented health and economic crisis, paralyzing entire countries, forcing governments and central banks to undertake massive fiscal and monetary stimuli. The good news came in the last days of the year, with the arrival of vaccines that promise to help fight the pandemic. Now, with the situation still out of control in most countries, we believe the ability to vaccinate the population, with all the logistical difficulties (ranging from the acquisition of doses, to the application of the same) will dictate the pace of the resumption of global economic activity. The maintenance of broad monetary stimuli in the main economies, added to expectations of important additional fiscal stimuli in the U.S., should boost economic activity once the pandemic is more controlled, in our view. Therefore, we believe that 2021 will be a year of strong recovery in global activity, which should reach pre-crisis levels between the end of 2021 and the beginning of 2022. With the resumption of economic activity, we expect commodity prices to continue to be pressured. We also expect Inflation to reappear in developed economies, although still at comfortable levels.

Source: Bloomberg, Santander.
Vaccines and China’s growth expected to support commodity market recovery

- Optimism about global growth to prevail in 2021, in our view.

We expect oil prices to pick up by mid-2Q21, as broad immunization against the virus feeds optimism about future demand and global economic recovery. In our view, global oil supply should remain sluggish, with production cuts adjusting for demand so as to keep the market in deficit. Meanwhile, despite the sustained rally in 2H20 supported by fundamentals – strong demand from China, weather risk from La Niña, and lower ending inventories forecast for 2020-21 – we expect agricultural commodities prices in general to lose momentum later in the year, albeit remaining still above pre-pandemic levels. We believe Chinese soybean buying is likely to decelerate as the country’s hog herd is rebuilt, while soybean production is set for a record high this year. We expect this supply response (increase in planted area) to current high prices to drag prices down by year-end.
After a slow start, we expect Brazil’s Covid-19 vaccination campaign to pick up

- Risks of vaccine delays should be limited to 1H21, in our view.

In spite of the uncertain near-term outlook for the pandemic – given the emergence of coronavirus variants and the shortage of vaccine supplies – we expect the vaccination pace to accelerate in 2H21, as local manufacturing partners start production and more vaccines become available. In our view, the vaccination pace will be behind schedule (Plano Nacional de Operacionalização da Vacinação) by 20%, meaning that 59% of the population will be vaccinated by end-2021. Considering an average efficacy of 60% (Butantan/Sinovac is 50% effective, while Fiocruz/AstraZeneca is 70% effective) and accounting for previous and future infection, we project that 48% of the population will be immune to the virus by December 2021, below the 60% herd immunity threshold.

Sources: Ministry of Health, Santander.
Important measures and reforms that could be implemented

- Beyond the question of vaccination, we believe certain measures and reforms are necessary to support the reduction of idiosyncratic risks. The fiscal agenda contains significant risks in its execution, in our view, so uncertainty will remain.

### Positive Measures That Could Be Implemented

<table>
<thead>
<tr>
<th>Budget law for 2021 in compliance with the spending cap rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum emergency fiscal measures</td>
</tr>
<tr>
<td>Advances in the important privatizations process</td>
</tr>
<tr>
<td>The new tax reform project, or CBS Law (Contribution on Goods and Services)</td>
</tr>
<tr>
<td>The autonomy of the Central Bank</td>
</tr>
<tr>
<td>The continuity of the modernization of regulatory frameworks</td>
</tr>
<tr>
<td>A balanced auction for 5G in communication and data</td>
</tr>
<tr>
<td>Some positive signs about the direction of administrative reform</td>
</tr>
</tbody>
</table>

### Potential Setbacks

- Possible creation of new mandatory expenses
- Permanent increases in the tax burden
- Approval of a new digital tax (CPMF)
- Approval of federal measures that imply leniency or moral hazard with fiscal adjustments
- Allocation of revenue not linked to public funds for other primary expenditures
- Paralysis of the reform agenda impacted by political disputes
- Salary increases for public servants
- Reduction in net revenue or greater transfers to states and municipalities

Source: Santander Brazil.
Fiscal accounts on a tightrope with the possible reintroduction of emergency aid

- An important debate will be the resumption of emergency aid, in our view. We expect that its reintroduction (due to the pandemic) will be at least partially balanced (not at the same time) by the approval of fiscal reforms – with possible headwinds in the political debate.

This year we believe Brazil will be walking a tightrope to avoid a further deterioration in the fiscal consolidation outlook. Although we expect headwinds in the fiscal debate, the most important aspect will be maintaining debt sustainability, which suffered a significant deterioration in 2020. Any change in this outlook could cause financial conditions to deteriorate, in our view.

**We believe that income transfers will be temporarily resumed in 2021, conditional on the deterioration of the pandemic.** We expect this to be done by extraordinary credit (not included in the spending cap). We project a total amount of BRL25 billion for four months, reaching 30 million beneficiaries not included in *Bolsa Familia*. We believe this extension will have as a counterpart (not at the same time) the approval of fiscal trigger measures to offset the increase in expenses and avoid affecting the debt trajectory – simultaneously offsetting the temporary breach in the spending cap, with the possibility of complying with the rule by 2024. We believe the government will comply with the spending cap rule in 2021 (with severe discipline) and in 2022.
Lingering (mobility and wage) impacts of the pandemic to slow the speed of recovery

- After a weak start in 1Q21, we expect progress in vaccination and a rise in mobility to reignite economic activity from 2Q21 onwards.

The upsurge in the pandemic observed in recent weeks will likely lead to a rollback in the economy's reopening process, in our view, with an unavoidable deterioration in mobility relative to 4Q20, although mobility should be above the worst periods of the crisis. Regarding 1Q21, we believe services related to social interaction, which were expected to be the main drivers of the recovery, will be hard hit; we will also see the first signs of the materialization of the fiscal cliff due to the withdrawal of emergency aid, with a considerable impact on the income-led retail sales segments. On the other side, we believe the manufacturing industry will face an inventories recomposition in 1H21, while the building sector should keep improving. From 2Q21 onward, progress in the massive vaccination campaign in conjunction with a new (smaller) round of emergency aid and with the improvement in mobility should ignite a gradual resumption of economic activity. The available credit supply, a recovery in confidence, and the spending of precautionary savings accumulated during the crisis savings should also contribute positively to economic activity.
Normalization in labor force expected to lead to higher unemployment rate

- After the sharp drop in the labor force in 2020, we expect a normalization process (more people searching for jobs) in 1H21 that will lead to an increase in the unemployment rate.

We expect the unemployment rate to have two distinct behaviors in 1H21 and 2H21. In the first half, the labor force should gradually recover to pre-crisis levels, following the (gradual) reopening process expected for the period, and the halting of the emergency aid in the first months of 2021. On the other hand, we expect employment to have a poor performance in 1Q21, with social distancing measures still in place and persistently high levels of uncertainty, related to both the pandemic evolution and fiscal concerns, which will limit job creation. In 2H21, as the labor force recovers to pre-crisis levels and reduces its growth rate, we expect a gradual drop in the unemployment rate. As a higher proportion of the population is immunized, the rise in mobility levels should add momentum to the labor market recovery rate, in our view. However, we do not expect the employed population to return to pre-crisis levels before 2Q22. We also foresee a more precarious situation in the labor market in the post-pandemic period, with a higher degree of informality and lower real wages.

Sources: IBGE, Santander forecasts.
Drop in “expanded” real wage bill, despite a new round of emergency aid

The reintroduction of the emergency aid and anticipation of some cash transfers through social benefits will raise the “expanded” real wage bill for 2Q21, in our view. However, we believe the full year 2021 figure should still represent a drop vs. 2020.

We estimate the “expanded” wage bill rose 3.1% adjusted for inflation for full year 2020 compared to 2019. In the counterfactual simulation without considering the government transfers, we calculate a 6.3% drop in the real wage bill, so that the benefits more than offset the estimated cyclical drop caused by the pandemic, with an increase of almost 9.5 p.p. of positive impulse.

For 2021, we consider a reintroduction of the emergency aid from March to June, which, together with an anticipation of cash transfers through social benefits, should lead to a high level for the “expanded” wage bill. In 2H21, we believe the gradual recovery of labor market should be reflected in the real wage bill, as represented in the dark grey bars of the chart. **We expect a 6.6% drop in the “expanded” real wage bill for 2021.**
Credit as a driver of economic activity

- We expect bank credit to companies to decelerate from 2020 levels, but capital markets have significant room for growth.

For 2021, we see broad credit growth as a driver of economic activity, as the economy gets back on track. Bank lending for households has recovered from the worst of the Covid-19 pandemic. Looking ahead, we see credit for this segment having the potential to resume growth, driving economic activity. Low interest rates should keep the housing market afloat. In our view, the risk here is consumer indebtedness, currently on an upward trajectory, as rising delinquency rates could prompt banks to tighten credit to households. For companies, we expect a slowdown in bank credit, since in 2020 firms relied heavily on emergency credit programs (PEAC, Pronampe) and working capital to bridge short-term liquidity needs. On the other hand, capital markets may benefit from domestic investors – weary of low interest rates on savings and piling into the equities market – and foreign investors’ risk appetite, depending on macro developments, especially linked to fiscal decisions.

### Total corporate financing (inflation adjusted, BRL billion)

<table>
<thead>
<tr>
<th>Year</th>
<th>Equities</th>
<th>Fixed Income</th>
<th>Foreign Market</th>
<th>SFN</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>2,000</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
<tr>
<td>2015</td>
<td>1,750</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
<tr>
<td>2016</td>
<td>1,500</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
<tr>
<td>2017</td>
<td>1,250</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
<tr>
<td>2018</td>
<td>1,000</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
<tr>
<td>2019</td>
<td>750</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
<tr>
<td>2020e</td>
<td>500</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
<tr>
<td>2021e</td>
<td>250</td>
<td>1,500</td>
<td>750</td>
<td>250</td>
</tr>
</tbody>
</table>

SFN - exclude *conta garantida, cheque especial* (overdraft) and credit card. Foreign Market - bonus, MTNs and securities. Fixed Income - Debentures, commercial papers, LFs, CRAs, CRIs e FIDCs. Equity - IPO and follow-on.

Sources: BCB, Anbima, Santander.
A benign inflation scenario, but with a risky path

- Inflation below the target, but with a top down (risky) convergence, in our view.

The benign inflation scenario is mainly based on: (i) anchored inflation expectations and (ii) broad idleness in the economy. The recrudescence of the pandemic alongside difficulties with the vaccination process acts to curb demand, keeping prices (particularly of services) well behaved, while anchored expectations prevent higher impacts of inertia. However, on the supply side, we expect inflation of costs to pressure IPCA. The ongoing global recovery suggests a support for already high commodity prices, preventing a stronger cooling down of food prices, in our view. For industry, commodities are also a source of pressure, and we expect the global supply chain to continue to suffer from the pandemic effects for a while. On top of that, the riskier fiscal scenario should keep the BRL at depreciated levels. As a result, we believe food and industrial goods prices should prevent a sharper deceleration of IPCA, and administered prices should also be a source of upward pressure, while the gradual recovery of services is one of the anchors of the benign inflation scenario.
A less accommodative monetary policy stance in 2021 and 2022

- The BCB is signaling discomfort about the “extraordinary” level of stimulus, with the Selic policy rate at 2.00%. The BCB sees a reversal of deflationary shocks and falling expectations seen early in the pandemic, as well as a reduction in economic slack.

In the minutes of the January Copom policy meeting, the BCB used a more hawkish tone and signaled urgency about the removal of stimulus. Although the authority’s baseline scenario projects inflation close to mid-target in 2021 (3.60% vs. 3.75% target) and in 2022 (3.4% vs. 3.50% target) assuming hikes starting in 2H21, the Copom believes the fiscal risks generate an upward bias to these estimates and justify an earlier move.

The BCB has grown worried about the inflation outlook after a slate of uncomfortably high readings for underlying inflation in recent months, and following “better than expected” activity numbers in 4Q20.

The exact timing, pace, and magnitude of hikes will hinge particularly on the materialization of uncertainties relative to the pandemic (immunization), activity (mobility), inflation (core), and fiscal policy (stimulus).

As we forecast a slower erosion of economic slack and moderate fiscal stimulus, our baseline scenario (now under revision) will anticipate hikes into 2021 but incorporate a slower pace of tightening into 2022. Our forecasts will move closer to the (increasingly hawkish) consensus.
Spoiling the opportunity to fix the roof

- The continuation of constructive global conditions should help the BRL to register some strengthening this year, but uncertainties regarding the domestic fiscal and institutional frameworks should limit the room for a more substantial move, in our view.

We expect global financial conditions to remain constructive for the BRL, with commodity prices and the international trade flow still suggest a rising trend, in tandem with the maintenance of favorable liquidity conditions by the monetary authorities of most advanced economies. These circumstances tend to favor the strengthening of emerging market currencies, and we do not expect the BRL to be an exception. However, we believe the recent performance of the BRL has been less striking than we would expect under the current global circumstances, which has led us to believe that idiosyncratic issues – mainly related to fiscal policy – have prevented the country from taking full advantage of these auspicious conditions abroad.

Previously, we expected the non-extension of the emergency aid into 2021 and compliance with the constitutional spending cap rule to reduce the level of uncertainty regarding short-term risks to the conduct of fiscal policy, while the resumption of debates on constitutional reforms would play a similar role regarding medium-term risks. Nonetheless, recent developments on the pandemic front have increased the probability of the implementation of new (albeit temporary) emergency aid and blurred the horizon for discussing structural reforms. So, domestic conditions should continue to prevent the more substantial BRL strengthening that we previously expected.
Thank you.

Our purpose is to help people and businesses prosper.

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

Simple Personal Fair

Santander

Brazil Macroeconomic Research Team

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

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

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

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

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

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

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

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

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

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

### CONTACTS / IMPORTANT DISCLOSURES

<table>
<thead>
<tr>
<th>Brazil Macro Research</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Ana Paula Vescovi*</td>
<td>Chief Economist</td>
</tr>
<tr>
<td>Mauricio Oreng*</td>
<td>Head of Macro Research</td>
</tr>
<tr>
<td>Jankiel Santos*</td>
<td>Economist – External Sector</td>
</tr>
<tr>
<td>Italo Franco*</td>
<td>Economist – Fiscal Policy</td>
</tr>
<tr>
<td>Daniel Karp Vasquez*</td>
<td>Economist – Inflation</td>
</tr>
<tr>
<td>Tomas Urani*</td>
<td>Economist – Global Economics</td>
</tr>
<tr>
<td>Lucas Maynard*</td>
<td>Economist – Economic Activity</td>
</tr>
<tr>
<td>Felipe Kolinda*</td>
<td>Economist – Credit</td>
</tr>
<tr>
<td>Gabriel Couto*</td>
<td>Economist – Special Projects</td>
</tr>
<tr>
<td>Gilmor Lima*</td>
<td>Economist – Modeling</td>
</tr>
<tr>
<td>Global Macro Research</td>
<td></td>
</tr>
<tr>
<td>Maciej Reluga*</td>
<td>Head Macro, Rates &amp; FX Strategy – CEE</td>
</tr>
<tr>
<td>Juan Cerruti *</td>
<td>Senior Economist – Argentina</td>
</tr>
<tr>
<td>Ana Paula Vescovi*</td>
<td>Economist – Brazil</td>
</tr>
<tr>
<td>Juan Pablo Cabrera*</td>
<td>Economist – Chile</td>
</tr>
<tr>
<td>Guillermo Aboumrad*</td>
<td>Economist – Mexico</td>
</tr>
<tr>
<td>Piotr Bielski*</td>
<td>Economist – Poland</td>
</tr>
<tr>
<td>Mike Moran</td>
<td>Head of Macro Research, US</td>
</tr>
<tr>
<td>Fixed Income Research</td>
<td></td>
</tr>
<tr>
<td>Juan Arranz*</td>
<td>Chief Rates &amp; FX Strategist – Argentina</td>
</tr>
<tr>
<td>Mauricio Oreng*</td>
<td>Senior Economist/Strategist – Brazil</td>
</tr>
<tr>
<td>Juan Pablo Cabrera*</td>
<td>Chief Rates &amp; FX Strategist – Chile</td>
</tr>
<tr>
<td>Equity Research</td>
<td></td>
</tr>
<tr>
<td>Miguel Machado*</td>
<td>Head Equity Research Americas</td>
</tr>
<tr>
<td>Alan Alanis*</td>
<td>Head, Mexico</td>
</tr>
<tr>
<td>Andres Soto</td>
<td>Head, Andean</td>
</tr>
<tr>
<td>Claudia Benavente*</td>
<td>Head, Chile</td>
</tr>
<tr>
<td>Walter Chiavesio*</td>
<td>Head, Argentina</td>
</tr>
<tr>
<td>Daniel Gewehr*</td>
<td>Head, Brazil</td>
</tr>
<tr>
<td>Electronic</td>
<td>Bloomberg SIEQ &lt;GO&gt;</td>
</tr>
<tr>
<td></td>
<td>Reuters Pages SISEMA through SISEMZ</td>
</tr>
</tbody>
</table>