

Brazil Macro Compass**Flat (and Disappointing) Industrial Production in 1Q18**

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What's New: Yet Another Disappointing Economic Activity Indicator

March industrial production data surprised to the downside: Monthly (seasonally adjusted) production was down 0.1%, which translates into a flat quarterly performance (we expected +0.6% and 0.3%, respectively). Most of the deceleration in 1Q18 versus 3Q17 came from intermediate and durable goods (to -1.6% q/q from +1.5% and to +2.7% from +6.7%, respectively). Production of capital and non-durable goods expanded at a moderate pace (+1.6% and +1.3% q/q, respectively). This result reinforces a downward bias we added to our 2018 GDP growth forecast (currently at 3.2%) following the February releases. 1Q18 GDP will be released on May 31.

Upcoming Data: April Inflation, March Retail Sales

April CPI inflation data will be released on Thursday. We expect monthly headline inflation at 0.26%, which would keep 12-month inflation at 2.8%, significantly below the midpoint of the target pursued by the Central Bank (BCB). This will be the last release before the next monetary policy meeting, on May 16. We believe that BCB will follow market consensus and deliver a 25-bps cut on the Selic rate (to 6.25%), thus ending the long and steep easing cycle that began in October 2016.

March retail sales will be released next Friday. We expect monthly change at -0.1% (for the core indicator), with y/y growth accelerating to 5.5% (from 1.3% in February).

In-Depth Research: Impact on Brazil of an Escalation in Protectionism

In our most recent report, *Infinite (Trade) War: Does It Matter for Brazil?* (May 2, 2018), we ran econometric models to estimate the impact on Brazil of a global escalation in protectionism (U.S. increasing tariffs on all Chinese imports by 25%, reciprocated by China). **As we expected, given the low degree of openness of the Brazilian economy, most of the effects are indirect, through a deterioration in financial market variables: of the 1-pp contraction in 2019 GDP growth we would expect under that scenario, 0.9 pp would be result of increased volatility and risk aversion, along with lower commodity prices, whereas only 0.1 pp would derive from lower export revenue.**

Political Agenda: Congress Back to Work after May 1 Holiday

Following a slow week after the May 1 holiday, the Lower House is expected to resume work on its economic agenda next week. **In an interview with *Agência Estado* last Thursday (April 26), Rodrigo Maia, the speaker of the house, said that he plans to put the *Cadastro Positivo* (credit bureau) bill to a floor vote next Tuesday (May 8).** The electoral campaign remains on the back burner, with no major national polls scheduled to be released.

Chart of the Week: Public Investment and Capital Formation

Researchers Rodrigo Orair (from the Senate's Independent Fiscal Institution and IPEA) and Sergio Gobetti (IPEA) recently updated their long-run time series on public investment. **According to their data, public investment in 2017 was the lowest in the 70 years covered by their research, amounting to only 1.85% of GDP (1.16% excluding state-owned firms).** Gross fixed capital formation, at 15.6% of GDP, was the lowest since 1965.

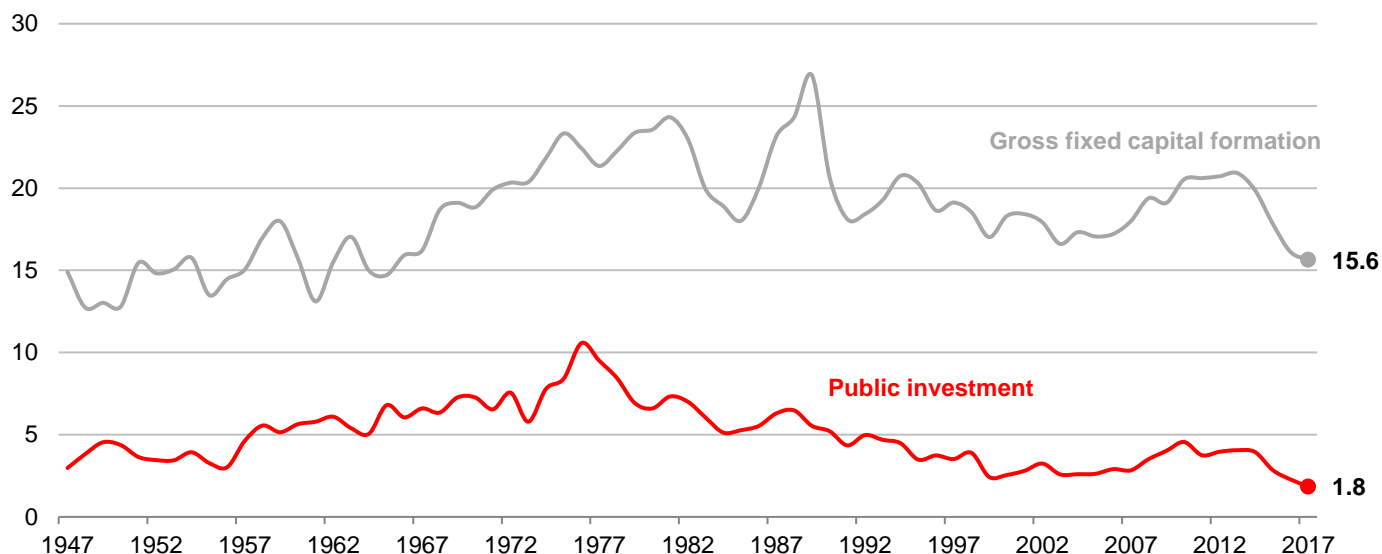
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Brazil: Public Investment (Including State-Owned Firms) and Gross Fixed Capital Formation, % of GDP



Sources: Orair & Gobetti, Observatório de Política Fiscal FGV/IBRE, Santander.

Number of the Week

R\$1.16bn

The Brazilian Congress approved this week a BRL 1.16 billion (USD 328 million) outlay (from the unemployment insurance fund) to make up for defaults from Venezuela and Mozambique on loans from BNDES and a global investment bank. The loans were insured by a fund controlled by the Finance Ministry, but were not provisioned in this year's budget.

Quote of the Week

The voter will actually wake up for the election and will begin to determine the vote, especially this year, when everything is so messed up, [by] watching TV. I think the TV campaign may matter even more than in the last election.

— **Mauro Paulino**, Datafolha's chief executive, in interview with *Valor* (May 4, 2018)

What We've Been Reading

- "From Janitor to Chief Justice: Could Joaquim Barbosa be Brazil's Next President?" by Shasta Darlington (*The New York Times*). A short profile of a possible outsider in the presidential race.
- *The peculiar insertion of Brazil into global value chains*, by Julia Callegari, Tatiana Massaroli Melo, and Carlos Eduardo Carvalho (*Review of Development Economics*). Brazil has been failing to use imports (of both goods and capital) to add value to its exports and increase competitiveness.
- "Mario Vargas Llosa explains why his politics changed," by Michael Reid (*The Economist*). "He thinks that the corruption scandals linked to Odebrecht, a Brazilian construction firm, have 'rendered a great service' and will help cleanse the region's democracies of corruption by exposing it." The companion interview with Vargas Llosa is also worth reading.
- "In Brazil, patients risk everything for the 'right to beauty'," by Alvaro Jarrin (*The Conversation*). The Brazilian government subsidizes nearly half a million plastic surgeries every year.



Recent Publications (Available on Our Website)

- *Infinite (Trade) War: Does It Matter for Brazil?* (May 2, 2018)
- *Stickernomics – What Do the Prices of Soccer Stickers Around the World Tell Us About Exchange Rates* (April 24, 2018)
- *Lower for Longer: We Expect 2019 Year-End Selic at 7.5%* (April 12, 2018)
- *Falling Interest Rates Leading to BRL Weakness* (March 28, 2018)
- *NPLs Improving More Than Meets the Eye* (March 26, 2018)
- *TJLP: Less Discretion, More Volatility?* (March 19, 2018)



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