

Brazil Macro Compass

Despacito: Recent Data Point to a Slow Recovery

Luciano Sobral*
 lusobral@santander.com.br
 +5511 3553 3753

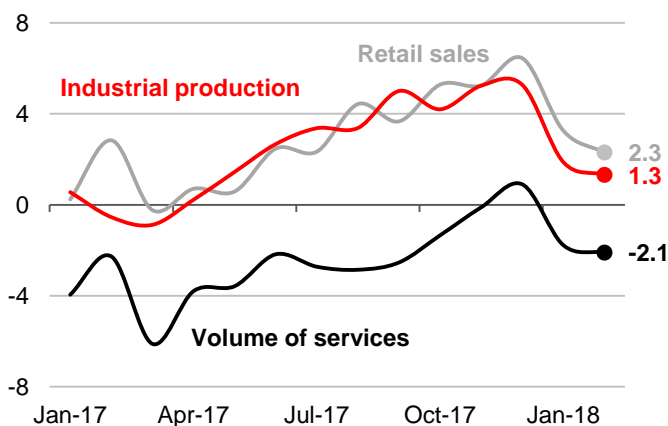
Chart of the Week: Decelerating Recovery

February data on retail sales and volume of services, released this week, confirmed a slowdown in the pace of the economic recovery, as already suggested in the industrial production numbers of that same month, released last week. All three main IBGE monthly indicators from February frustrated market consensus, adding to two negative surprises in January and suggesting relatively weak 1Q18 GDP growth. We attribute a negative bias to both our 2018 full-year and first quarter GDP growth forecasts, currently at 3.2% and 0.6% (q/q), respectively. Bear in mind that 3.2% annual growth requires 1.0% average quarterly growth, given the statistical effect (carry over) from 2017.

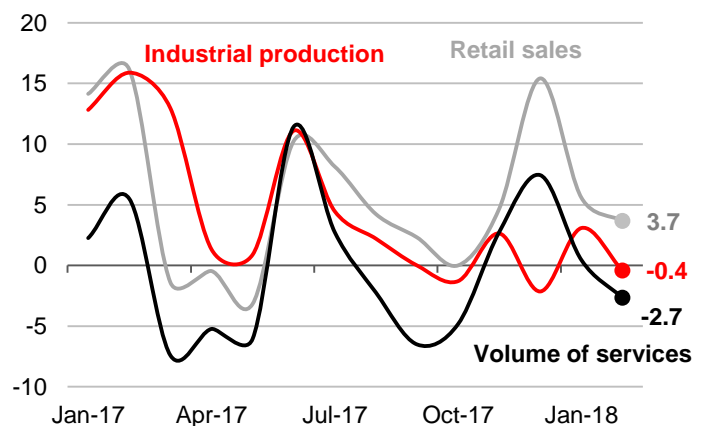
Persistent economic slack is one of the factors that led us to revise downwards our 2019 overnight rate forecast (see our “In-Depth Research” section on the following page).

Brazil – Economic Activity Indicators, Monthly Data

Year-on-Year Changes (%)



Annualized 3-Month Change (Seasonally Adjusted, %)



Sources: IBGE, Santander.

Political Agenda: Polls and New Attempts to Move Forward With the Economic Agenda

Datafolha, one of Brazil’s most important pollsters, is expected to release a new presidential poll next Sunday (the poll was registered in the Electoral Court on Monday, with 4,260 interviews conducted between Wednesday and Friday). This will be the first national poll to be published after former president Lula’s arrest and the deadline for outsiders to join political parties.

There were few advances in the legislative agenda this week. The *cadastro positivo* (credit bureau) bill was discussed, but a floor vote was obstructed by leftist deputies. The Central Bank independence proposal was not voted upon as well, but an April 13 article in *O Globo* reports that the economic team and the Speaker of the House came to an agreement on some minutiae of the bill and that it is ready for a vote next week. Its approval, however, will depend on successful negotiations with centrist parties, in our view.

IMPORTANT DISCLOSURES/CERTIFICATIONS ARE IN THE “IMPORTANT DISCLOSURES” SECTION OF THIS REPORT.

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What's New: Inflation Remains Low

March CPI inflation, released on Tuesday, was in-line with our expectation, at 0.09% m/m. Food price deflation remains surprisingly persistent, with prices falling 4.3% y/y. Core inflation also decelerated (to 2.9% from 3.2% in February), confirming our view that the Central Bank can comfortably keep its expansionary policy for longer than we previously expected (see “In-Depth Research” below). We reiterate our 12-month CPI inflation forecast of 3.5% at the year end.

We comment on the economic activity releases in the “Chart of the Week” above.

In-Depth Research: Lower 2019 Selic Rate

In *Lower for Longer: We Expect 2019 Year-End Selic at 7.5%* (April 12, 2018), we revised our 2018 and 2019 unemployment rate forecasts upward and cut our YE2019 Selic rate estimate to 7.5% (from 8.5%). Besides the slow economic recovery, three other factors should allow for a longer period of stimulative monetary policy: a deeper and longer-lasting-than-expected food price deflation, the transmission of current low inflation rates to future inflation (through indexed contracts), and Brazil's Central Bank improved credibility. Risks to our scenario include a sharp deterioration in financial markets and a reversal of the current responsible fiscal and monetary policies.

Upcoming Data: February GDP Proxy, April Inflation Preview

Brazil Central Bank releases on Monday its monthly GDP proxy (IBC-Br) for February, which should confirm the weak performance of other indicators (see “Chart of the Week” below), in our view. We expect y/y growth to decelerate to 0.7% (from 2.97% in January). April's inflation preview (IPCA-15) should show monthly inflation at 0.25%, leading to a further deceleration in the 12-month price change (to 2.8%, from 2.9% in March official index).

Number of the Week

9,000

Brazil Supreme Court examined 9,000 *habeas corpus* requests last year. The U.S. and Germany's highest courts rule on less than 10 of those requests per year, according to Justice Luís Roberto Barroso.

Quote of the Week

I'm not a human being anymore. I'm an idea.

— **Former President Lula**, in his speech before turning himself in to the Federal Police last Saturday.

What We've Been Reading

- “The Death of the PT or life after Lula?”, by Grant Burrier (*Global Americans*). What are the possibilities for the Workers' Party?
- “A Former President Goes to Prison”, by Diogo Costa and Magno Karl (*The Wall Street Journal*). It is now up to electors to deepen corruption fighting in Brazil, the authors argue.
- “Brazil's Right Comes Roaring Back as Lula Starts Prison Sentence, by Samy Adghirni and Simone Preissler Iglesias (*Bloomberg*) and “Brazil Turns Rightward, Heralding New Chapter for Latin America”, by Samantha Pearson (*The Wall Street Journal*). Congress and people's preferences in Brazil seem to be leaning to the right.
- “The threat of impeachment can push presidents out the door. But there's a catch.”, by John M. Carey, Javier Corrales, Mariana Llanos, Leiv Marsteindretet, and Anibal Pérez-Liñán (*Monkey Cage*). Lessons from the recent cases of removed presidents in Latin America.
- *The dynamical structure of political corruption networks*, by Haroldo V. Ribeiro, Luiz G. Alves, Alvaro F. Martins, Ervin K. Lenzi, and Matjaž Perc (*Journal of Complex Networks*). An original study of corruption networks in Brazil, showing that they are usually small (rarely comprising more than eight people) and increasingly interconnected.
- “Brazil Debates Fate of Millions of Idled Donkeys”, by Luciana Magalhães (*The Wall Street Journal*). Donkeys, replaced with motorcycles, are among the victims of technological unemployment in Brazil.



Recent Publications (Available on Our Website)

- *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)
- *Food (Inflation) for Thought (2): Forecasts* (March 9, 2018)



CONTACTS / IMPORTANT DISCLOSURES

Macro Research

Maciej Reluga*	Head Macro, Rates & FX Strategy – CEE	maciej.reluga@bzwbk.pl	48-22-534-1888
Sergio Galván*	Economist – Argentina	sgalvan@santanderrio.com.ar	54-11-4341-1728
Maurício Molan*	Economist – Brazil	mmolan@santander.com.br	5511-3012-5724
Juan Pablo Cabrera*	Economist – Chile	jcabrera@santander.cl	562-2320-3778
Diana Ayala	Economist - Colombia	diana.ayala@santander.us	212-350-0979
Tatiana Pinheiro*	Economist – Peru	tatiana.pinheiro@santander.com.br	5511-3012-5179
Piotr Bielski*	Economist – Poland	piotr.bielski@bzwbk.pl	48-22-534-1888
Marcela Bensi6n*	Economist – Uruguay	mbension@santander.com.uy	5982-1747-5537

Fixed Income Research

Diana Ayala	Macro, Rates & FX Strategy – Latin America	diana.ayala@santander.us	212-407-0979
Juan Arranz*	Chief Rates & FX Strategist – Argentina	jarranz@santanderrio.com.ar	5411-4341-1065
Juan Pablo Cabrera*	Chief Rates & FX Strategist – Chile	jcabrera@santander.cl	562-2320-3778
David Franco*	Macro, Rates & FX Strategy – Latin America	david.franco@santanderargcb.com	44-207-756-6633
Aaron Holsberg	Head of Credit Research	aholsberg@santander.us	212-407-0978

Equity Research

Christian Audi	Head LatAm Equity Research	caudi@santander.us	212-350-3991
Andres Soto	Head, Andean	asoto@santander.us	212-407-0976
Walter Chiarvesio*	Head, Argentina	wchiarvesio@santanderrio.com.ar	5411-4341-1564
Nicolas Schild*	Head, Chile	nschild@santander.cl	5622-336-3361
Valder Nogueira*	Head, Brazil	jvalder@santander.com.br	5511-3012-5747
Pedro Balcao Reis*	Head, Mexico	pbalcao@santander.com.mx	5255-5269-2264

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