

**Brazil Macro Compass****Combine and Conquer: Time for Political Alliances**

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**Political Agenda: Party Conventions Allowed from July 20**

The presidential race in Brazil reaches an important stage next week: the period defined by the Electoral Justice for party conventions starts on July 20. Until August 5 parties can promote their conventions (although conventions are not mandatory) and are expected to make crucial decisions about launching their own candidacies or joining other parties in coalitions.

Coalitions have always been important in Brazil's recent democratic history: in a country that cover almost half of the continent, with many regions having little access to media and/or highly dependent on government transfers, coalition capillarity (quantity and influence of local power brokers) plays an important role in influencing voting. In addition, radio and television advertising quotas, another important campaign tool, are allocated by the government mostly according to the number of representatives from the parties in the various coalitions. Finally, after the Supreme Court prohibition on corporate donations in 2015, the bulk of campaign money is likely to come from public funds, whose allocation is also partially linked to party size. Therefore, the final structure of the coalitions, especially those involving relatively large parties that are not planning to launch their own presidential candidates, should be critically important for the elections' outcome.

The scenario gains in complexity when we add the factor that alliances for presidential elections are not necessarily replicated in elections at the state level (for state governors, senators, and Lower House representatives). Ultimately, each party needs to maximize its political influence after the elections, constrained by mixed regional interests, historical loyalties and rivalries, programmatic orientation, and other factors. History probably can provide some guidance (see our "Chart of the Week" on page 2), but an environment of eroding popularity of the political establishment, the absence of a clear incumbent among the candidates, and polls pointing to strong candidacies from small parties may result in unconventional arrangements.

Congress starts its winter recess on July 17, resuming its activities on August 1.

**What's New: Weak Retail Sales in May, as Expected**

Core retail sales fell 0.6% m/m in May, in line with our forecast (-0.5% m/m), with rising supermarket sales (+0.6% m/m, probably due to people stockpiling basic goods fearing a prolonged truckers' strike) preventing a worst outcome. However, broad sales, including vehicles and building materials, declined 4.9% m/m, with auto sales plunging 14.6% m/m. We expect a strong rebound in June data, although not fully offsetting the losses recorded in May. 2Q18 data so far points to GDP growth at 0.2% q/q, significantly below our forecast before the strike (0.8% q/q), but still compatible with our recently revised forecast for the full year of 2% growth (for more details, see *Truck Strike: A Preliminary Assessment*, May 29, 2018).

**Upcoming Data: May IBC-Br**

Brazil's Central Bank releases its monthly GDP proxy (IBC-Br) on Monday (July 16). We estimate that the deterioration caused by the strikes and already manifested in industry, retail, and services data should translate into a 2.3% m/m contraction in the index, in what would be the worst month for economic activity since July 2015. As we noted in "What's New" above, a strong rebound in June should keep 2Q18 GDP growth in positive territory, albeit at a slower pace than we expected previously.

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

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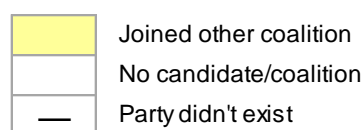
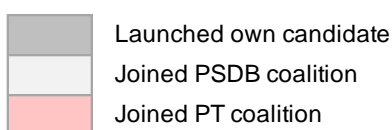
## Chart of the Week: Coalitions for Presidential Elections Through Time

Our “Chart of the Week” maps how party alliances evolved in the last six presidential elections. At least one historical pattern should hold this year: PT and PSDB launching their own candidates. It is also worth noting that the 2014 election was unusual in that most of the parties picked a side in the first round: between 1998 and 2010, several important parties decided not to support anyone formally, leaving more leeway for mixed arrangements according to regional convenience.

### Parties and Coalitions in the First Round of Presidential Elections

Party (current Lower House seats)	1994	1998	2002	2006	2010	2014
PT (61)						
MDB (51)						
PP (49)						
PSDB (49)						
DEM (43)						
PR (40)						
PSD (38)	—	—	—	—	—	
PSB (26)						
PRB (21)	—	—	—			
PDT (19)						
PODE (16)	—					
PTB (15)						
PROS (11)	—	—	—	—	—	
SD (11)	—	—	—	—	—	
PCdoB (10)						
PSC (9)						
PPS (8)						
PSL (8)	—					

Party (current Lower House seats)	1994	1998	2002	2006	2010	2014
PSOL (6)	—	—	—			
AVANTE (5)	—					
PATRI (5)	—	—	—	—	—	
PHS (4)	—					
PV (4)						
REDE (2)	—	—	—	—	—	—
PPL (1)	—	—	—	—	—	
PRP (1)						
PCB (0)						
PCO (0)	—					
PMN (0)						
PRTB (0)	—					
PSDC (0)	—					
PSTU (0)	—					
PTC (0)						
PMB (0)	—	—	—	—	—	—
NOVO (0)	—	—	—	—	—	—



Includes alliances made by parties under previous names and before mergers. Sources: Carreirão, Yan de Souza (2014). “O sistema partidário brasileiro: um debate com a literatura recente”. *Revista Brasileira de Ciência Política* n. 14, 255-295; Superior Electoral Court, Lower House, and Santander.

## Number of the Week

# 0

Brazil's Central Bank net (excluding the rollover of maturing swap contracts) intervention in the FX market has been nil since June 22, when the BRL was quoted at 3.77/USD.

## Quote of the Week

*There is no sense in putting a limit within the existing [spending] cap.*

— **Senator Romero Jucá**, MDB's national president, proposing an amendment to next year's budget that may allow civil servants to get wage increases (July 12, 2018, on Twitter).



## What We've Been Reading

- “Trump’s Protectionist Threat to Latin America,” by Laura Alfaro, Pablo Guidotti, Guillermo Perry, and Liliana Rojas-Suarez (*Project Syndicate*, July 10, 2018). Countries in Latin America should brace for the (mostly) indirect effects of the Sino-American trade war, the authors argue.
- “Will Brazil’s Next President Be a Far-Right Nationalist,” by Bruno Carazza (*Foreign Affairs*, July 12, 2018). The author evaluates the odds of Jair Bolsonaro in the presidential race.
- “Brazil’s Simmering Democratic Demise,” by Katie Hillegass (*War on the Rocks*, July 4, 2018). A bleak view of the expanding role of the military in Brazilian politics.
- “What Nobody Wants to Say About the Current Political Crisis in Brazil,” by Rodrigo R. Soares (*Brazil Talk*, July 4, 2018). “The Brazilian political class has not yet fully realized what is at stake in the coming years. If they do not get their act together and respond to popular demand by offering political change through institutional means, the change will take them by surprise.”

## Recent Publications (Available on Our Website)

- “*Lethal Weapon*”: *How Far Can the BCB Go with Swaps?* (June 15, 2018)
- *Rely on Fundamentals and Carry On* (June 8, 2018)
- *Truck Strike: A Preliminary Assessment* (May 29, 2018)
- *Copom Capitulates to Changing Balance of Risks* (May 16, 2018)
- *Monetary Policy: The Good Governance* (May 9, 2018)
- *Infinite (Trade) War: Does It Matter for Brazil?* (May 2, 2018)



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