

Brazil Macro Compass

A V-Shaped Recovery from the Truckers' Strike

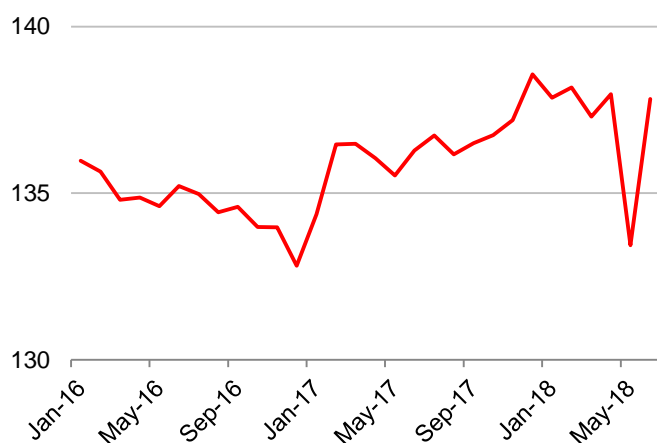
Luciano Sobral*
 lusobral@santander.com.br
 +5511 3553 3753

What's New: Economic Activity Rebounded in June

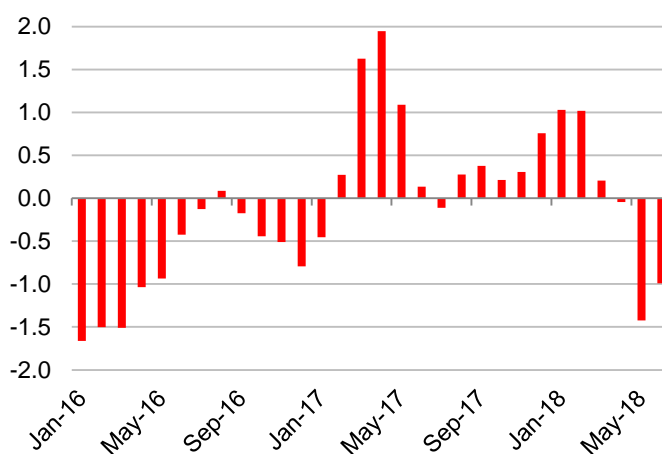
Brazil's Central Bank monthly GDP proxy (IBC-Br) rebounded strongly in June from the sharp contraction in May, which was caused mostly by the truckers' strike. The index rose 3.3% m/m (1.8% y/y), in line with our estimates. This performance reflects a disseminated recovery already present in other high-frequency indicators such as industrial production, retail sales, and services revenue.

However, June figures did not prevent a notably weak 2Q18, on average. On this comparison, IBC-Br moved to -1.0%, from +0.2% in 1Q18. Still, we believe that 2Q18 GDP data (to be released on August 31) will show modest (+0.2% q/q) growth (differences in methods for seasonal adjustment explain most of the divergence between the two indicators, which otherwise usually follow similar trends). This recovery pace is slightly slower than we expected a few months ago; accordingly, we assign a downward bias to our 2018 full year GDP growth forecast (currently at 2.0%).

IBC-BR – Level



IBC-Br – Three-Month Average Growth (%)



Sources: Brazil's Central Bank, Santander.

Upcoming Data: August Inflation Preview

August IPCA-15 is the most important economic indicator to be released next week (on August 23). We expect monthly inflation at 0.07% (4.24% y/y), vs. 4.53% y/y in July. Most of the retracing is explained by the dissipation of the effects of the May negative supply shock on fuel and foodstuff. We believe that inflation from August onward should align with the hypothesis that the exchange rate pass-through is relatively low, mostly because of the wide output gap. With that, we believe 2018 year-end inflation expectations (currently at 4.15%) should soon start to fall, strengthening our call for a flat Selic rate (at 6.5%) until 2H19.

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

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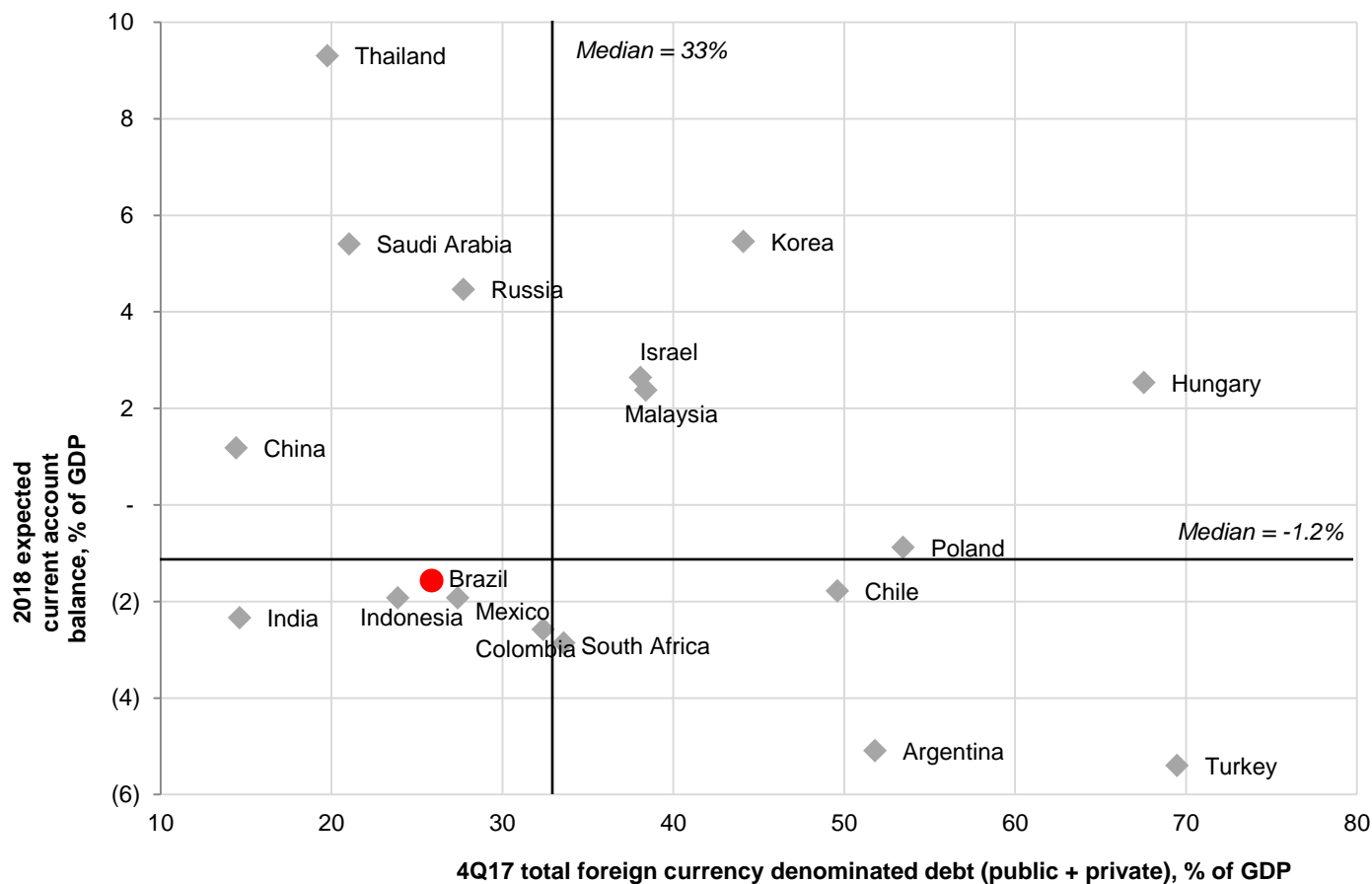
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Chart of the Week: Mapping External Vulnerabilities

In our “Chart of the Week” we tried to map the external vulnerabilities, which may be a source of market stress in an environment of tightening USD liquidity, of some important emerging economies. Argentina and Turkey stand out as the most fragile of the sample, with high current account deficits (>5.0% of GDP) and a high stock of debt denominated in foreign currency (surprisingly, Chile is in the same quadrant, although with much lower levels for both variables). Brazil, after substantial deleveraging since 2015, has relatively low external debt (26% of GDP), mostly concentrated in companies, and a narrow (but widening) current account deficit. Thailand, Saudi Arabia, China, and Russia are the least vulnerable countries, according to those criteria.

Selected Emerging Countries – Current Account Balance and External Debt



Sources: IIF (debt), IMF estimates (current account), Santander.

Political Agenda: The Long Wait Continues

At the deadline for candidate registration, PT confirmed former president Lula as head of its presidential bid, triggering a request from the chief prosecutor for the Electoral Court to nullify Lula’s registration on the basis of his confirmed conviction by a court of appeals. The request is expected to be examined by Justice Luís Roberto Barroso, vice-president of the Supreme Electoral Tribunal. The court has until September 17 to rule on candidacies, the same deadline by which candidates can resign and be replaced.

Most recent presidential polls continue to show similar results to that seen since June, with about a third of total voters not opting for any candidate. New national polls from Ibope and Datafolha, Brazil’s largest and most traditional pollsters, are scheduled to be released on August 20 and August 22, respectively. We believe that major shifts in vote intentions will happen only after TV and radio advertisements start to have an effect on voters. Broadcasting starts only on August 31 (for more information on the time allocated to each presidential candidate, see our report *Countdown to Elections Officially Begins*, August 10, 2018).



Number of the Week

BRL 425 million

João Amoêdo (NOVO) declared BRL 425 million (USD 109 million) in assets to the Electoral Justice, the highest among Brazil's presidential candidates. Former finance minister Henrique Meirelles came close, with BRL 377 million declared.

Quote of the Week

I'll be cautious to avoid campaigning for one or another [presidential candidate]. Even because people talk a lot about unpopularity. I don't even want to bother, let's say.

— **President Michel Temer**, in an interview with *Folha de S. Paulo* (August 16, 2018).

What We've Been Reading

- *Inequality Aversion, Populism, and the Backlash Against Globalization*, by Lubos Pastor and Pietro Veronesi (NBER Working Paper No. 24900, August 2018). A model and evidence examined by the authors conclude that more unequal countries, with higher financial development and current account deficits, are more vulnerable to populism.
- "Brazilians Denounce Their Leader, but Economists Offer Praise," by Paulo Trevisani (*The Wall Street Journal*, August 16, 2018). Temer's economic legacy is probably much more positive than what his approval ratings suggest.
- "Candidates Trash Election Results Before Brazil Even Votes," by Mario Sergio Lima and David Biller (*Bloomberg*, August 9, 2018). PT and Bolsonaro have already been questioning the legitimacy of the upcoming elections, for different reasons.
- "Will Brazilians Elect Their Own Donald Trump?" by Jessie Bullock (*The Global Anticorruption Blog*, August 10, 2018). Bullock argues that "a vote for Bolsonaro is not a vote for anticorruption."
- *Partisans, Antipartisans, and Nonpartisans: Voting Behavior in Brazil*, by David J. Samuels and Cesar Zucco (Cambridge University Press). A new book tries to explain how voting in Brazil has been structured around voters' sentiments for or against the Workers' Party (PT), the only one in the country to attract strong partisan identification.

Recent Publications (Available on Our Website)

- *The Power of Trade-Off* (August 2, 2018)
- *It's Not for a Lack of Credit – Part III: Delinquency, Way Better than it Seems* (July 20, 2018)
- *It's Not for a Lack of Credit – Part II: Companies* (July 20, 2018)
- *It's Not for a Lack of Credit – Part I: Individuals* (July 18, 2018)
- "Lethal Weapon": *How Far Can the BCB Go with Swaps?* (June 15, 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 Bensión*	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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