

# Brazil in election year

## Consumption-led cyclical recovery and necessary reforms

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The economic policy is in  
the right direction **and the**  
**risk perception is**  
**improving in overall**  
**terms...**



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- **Constitutional amendment: spending cap bill**
- **Labor and union reforms**
  - Flexibility
  - Low inertial inflationary risks
- **New BNDES lending rate (TLP)**
  - No more subsidies
  - Lower equilibrium interest rates
- **Reduction in public banks “activism” and earmarked credit on the economy**
- **Privatizations**
- **No public tariffs misalignment**

# BRAZIL 5-YEAR CDS

Basis points



Sources: Bloomberg, Bradesco

**The economy is improving.**  
Families and companies  
have deleveraged quite  
well



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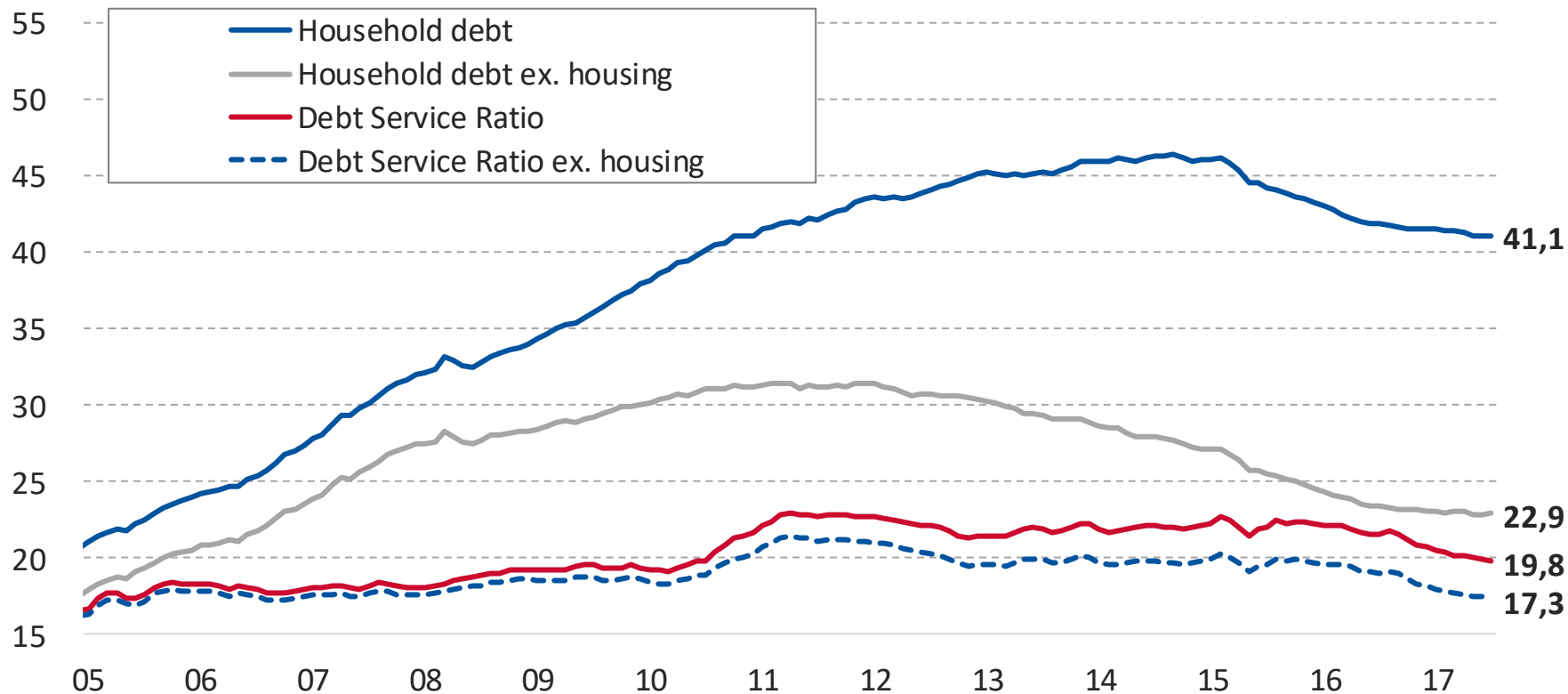
# CYCLICAL RECOVERY FACTS

Since 2017...

- **Deleveraging of families' balance sheet**
- **Low levels of inventories**
- **Low inflation and interest rates**

# HOUSEHOLD DEBT

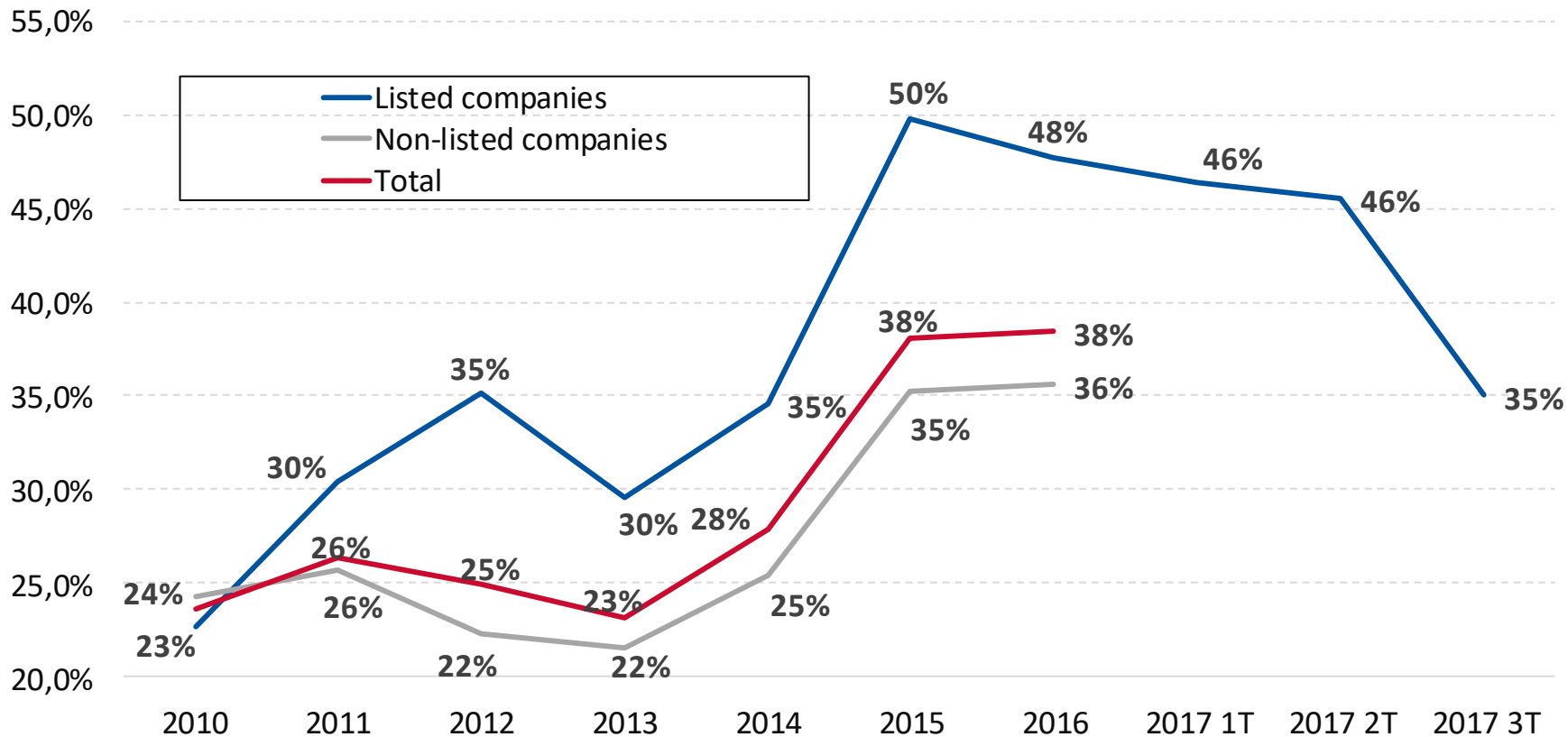
Debt service ratio as % of disposable income



Source: BCB, Bradesco

# CORPORATE DELEVERAGING

% of companies with EBITDA < Financial expenses

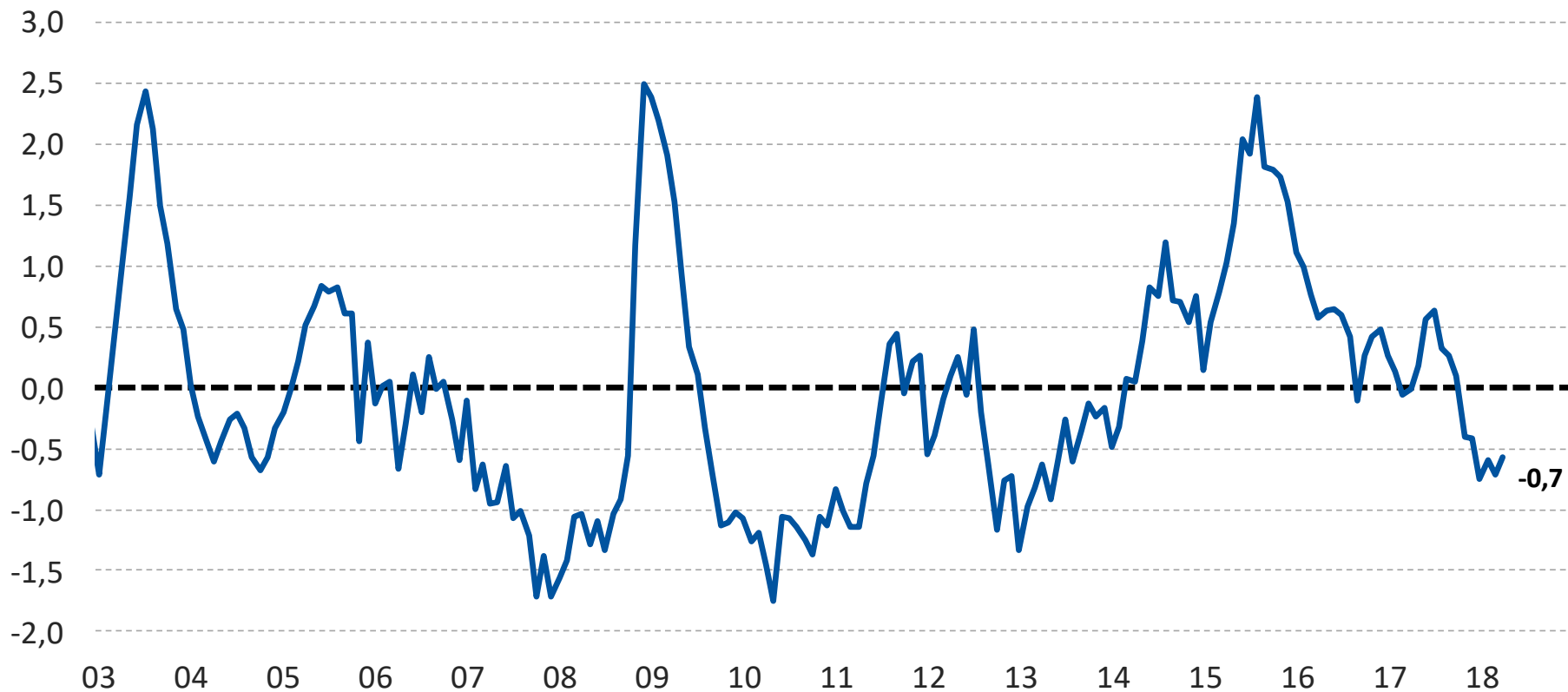


Source: CEMEC, Bradesco



# MANUFACTURING INVENTORIES

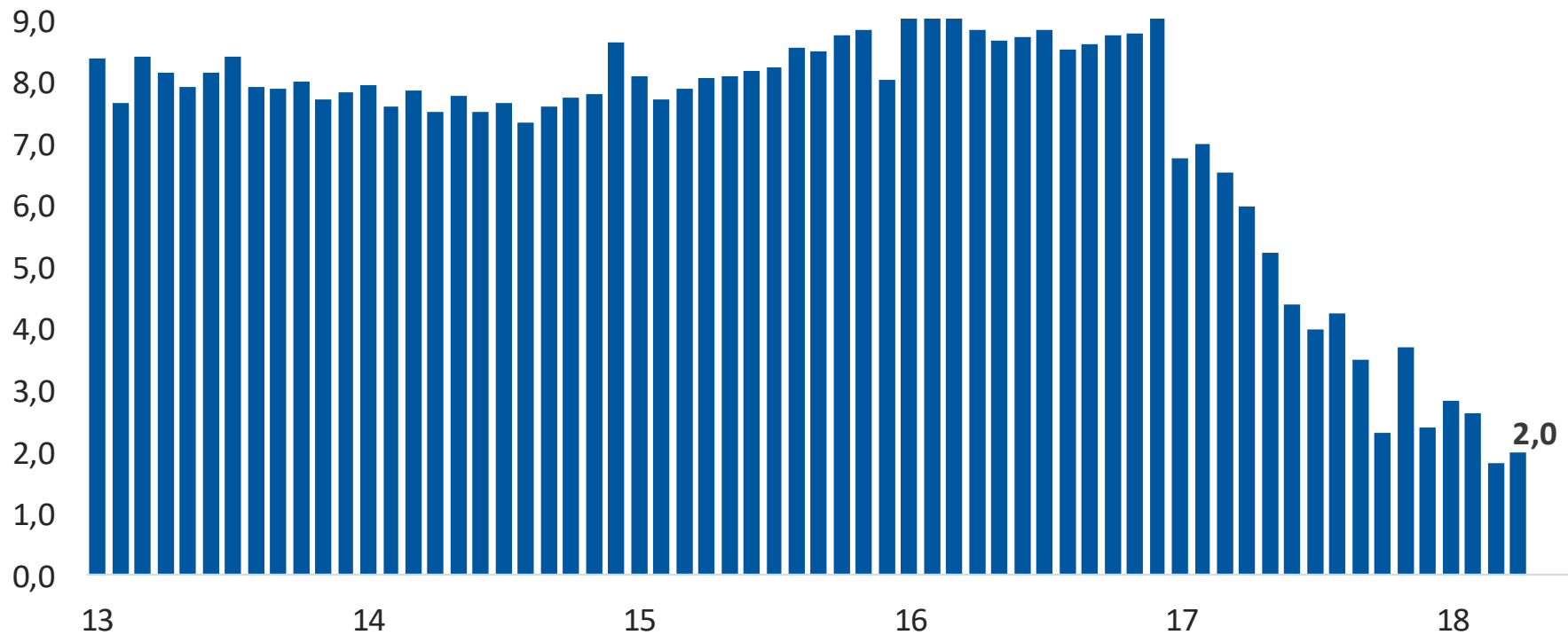
Seasonally adjusted



Source: FGV, Bradesco

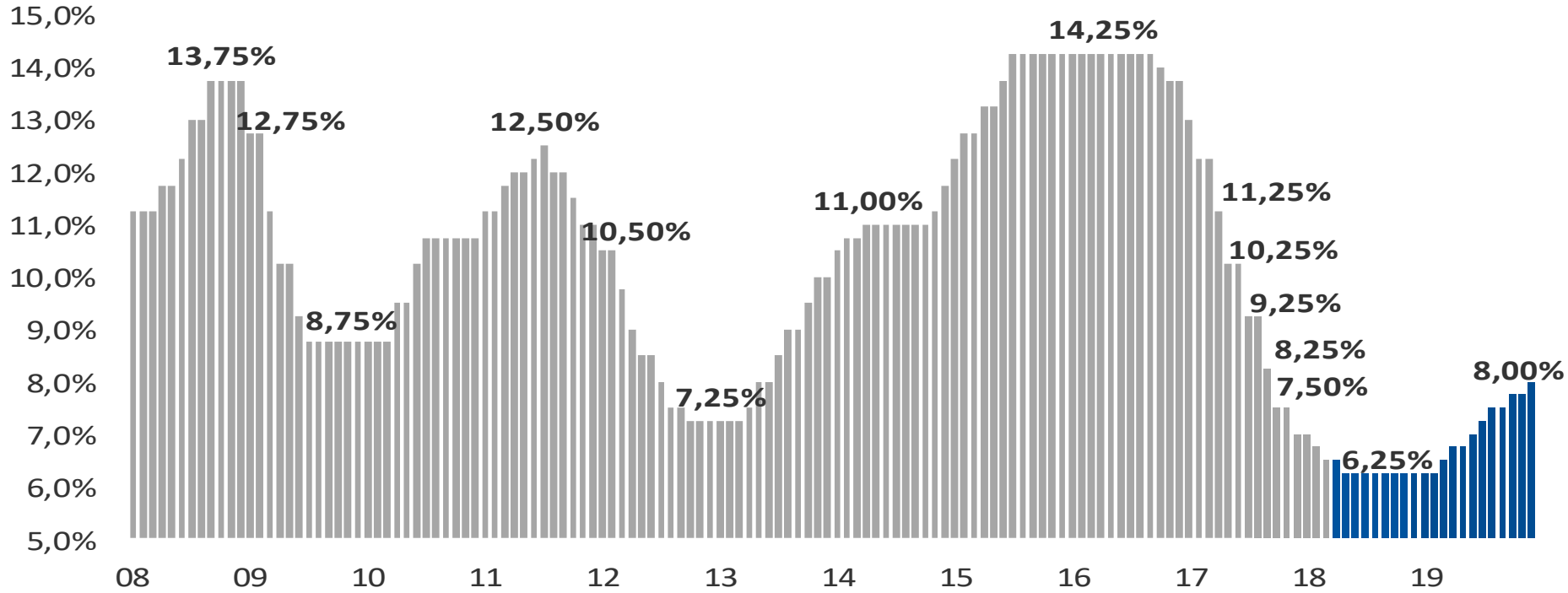
# WAGE INCREASES

Business survey, all sectors, %



# POLICY RATE

Selic, % p.a.



Source: BCB, Bradesco

**And the economy is  
starting to respond...**



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# REAL INCOME

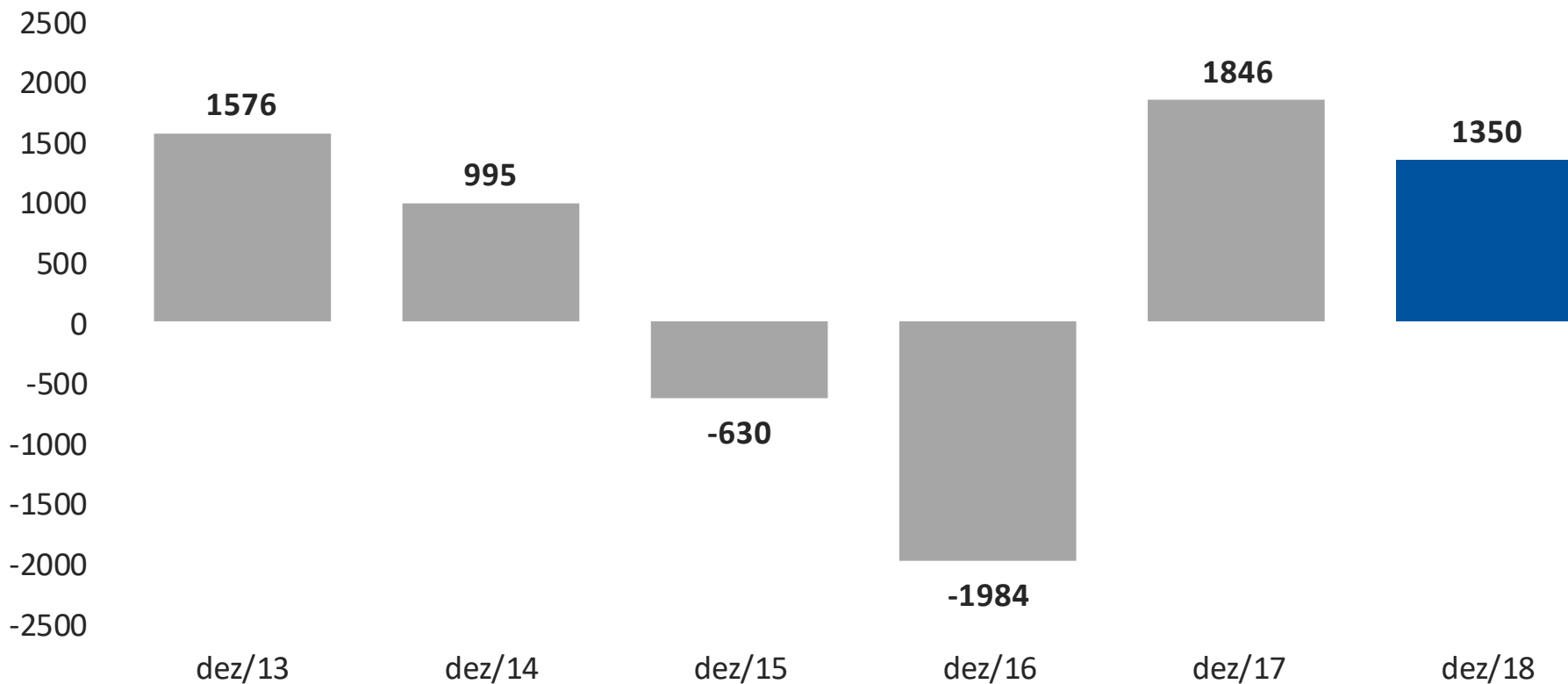
% Y/Y



Sources: BCB, Bradesco

# JOB CREATION

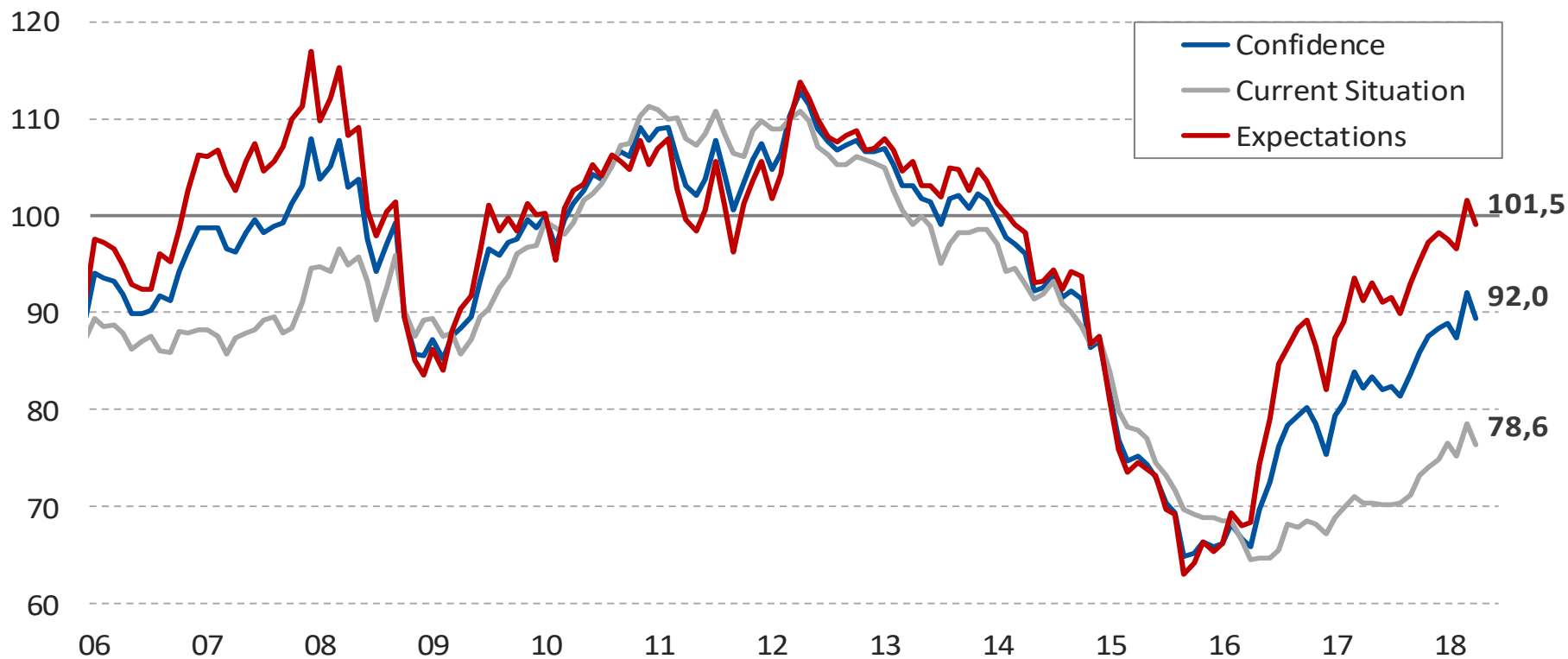
Thousands



Source: IBGE, Bradesco

# CONSUMER EXPECTATIONS

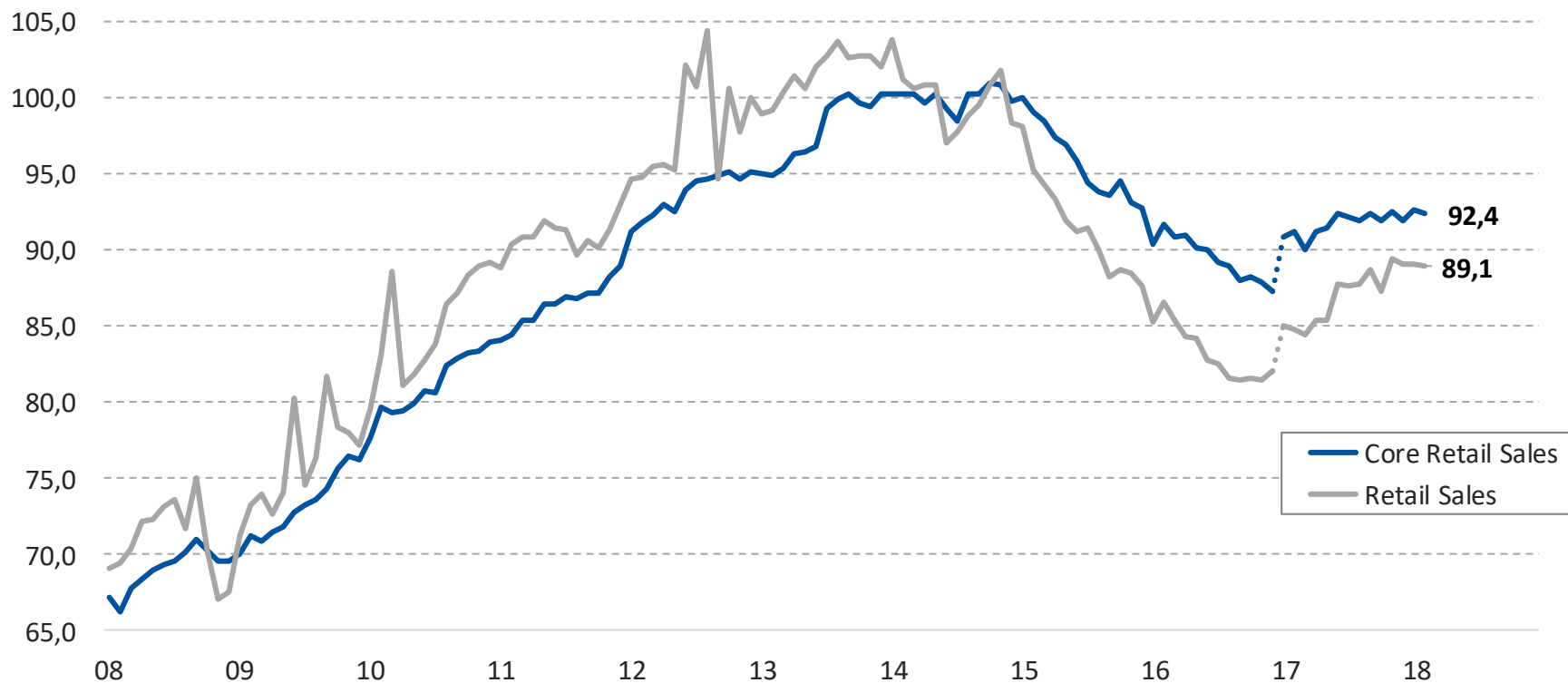
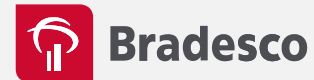
Seasonally adjusted



Sources: FGV, Bradesco

# RETAIL SALES

Real, level, 2011=100



Sources: IBGE, Bradesco

\* Core excludes vehicles and construction inputs



# INDUSTRIAL PRODUCTION

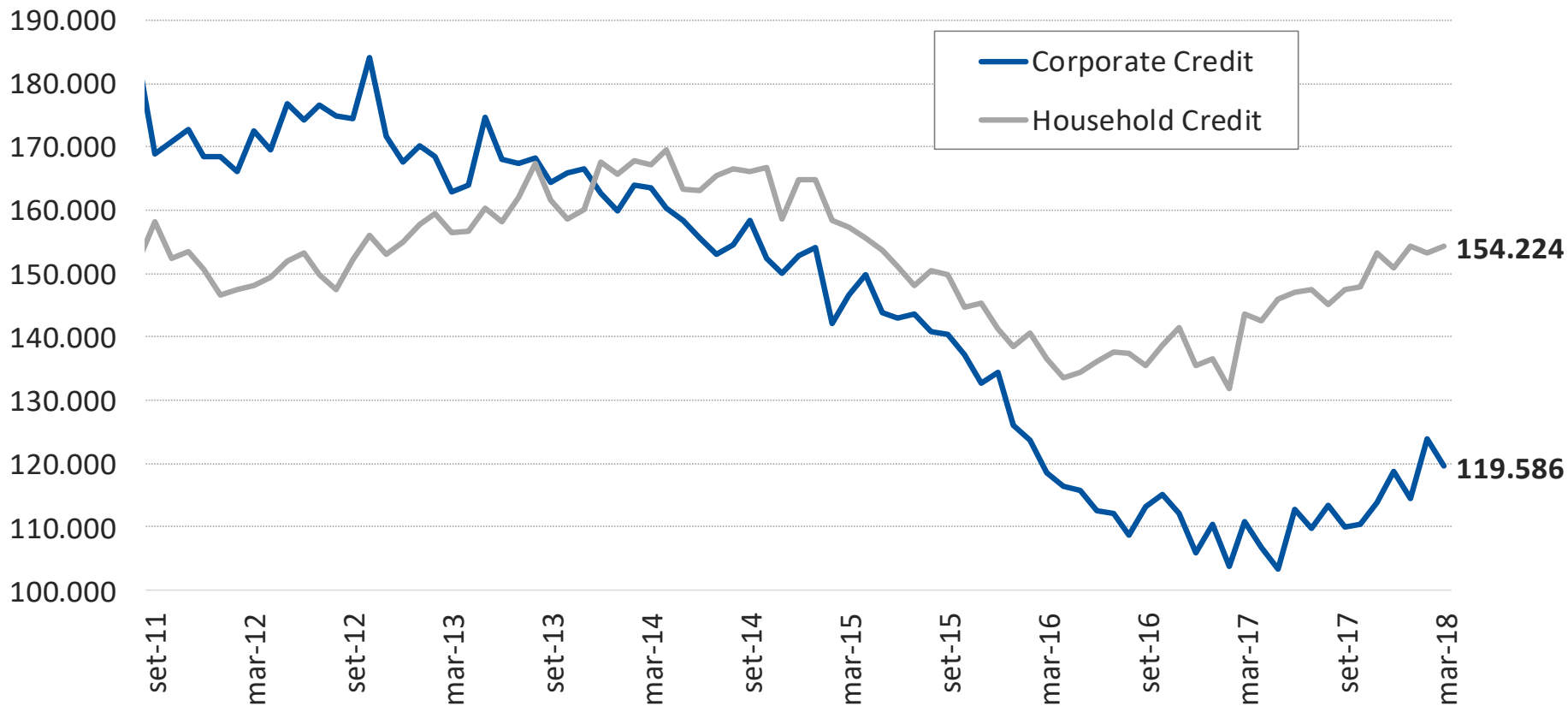
Level, seasonally adjusted



Source: IBGE, Bradesco

# CREDIT ORIGINATION

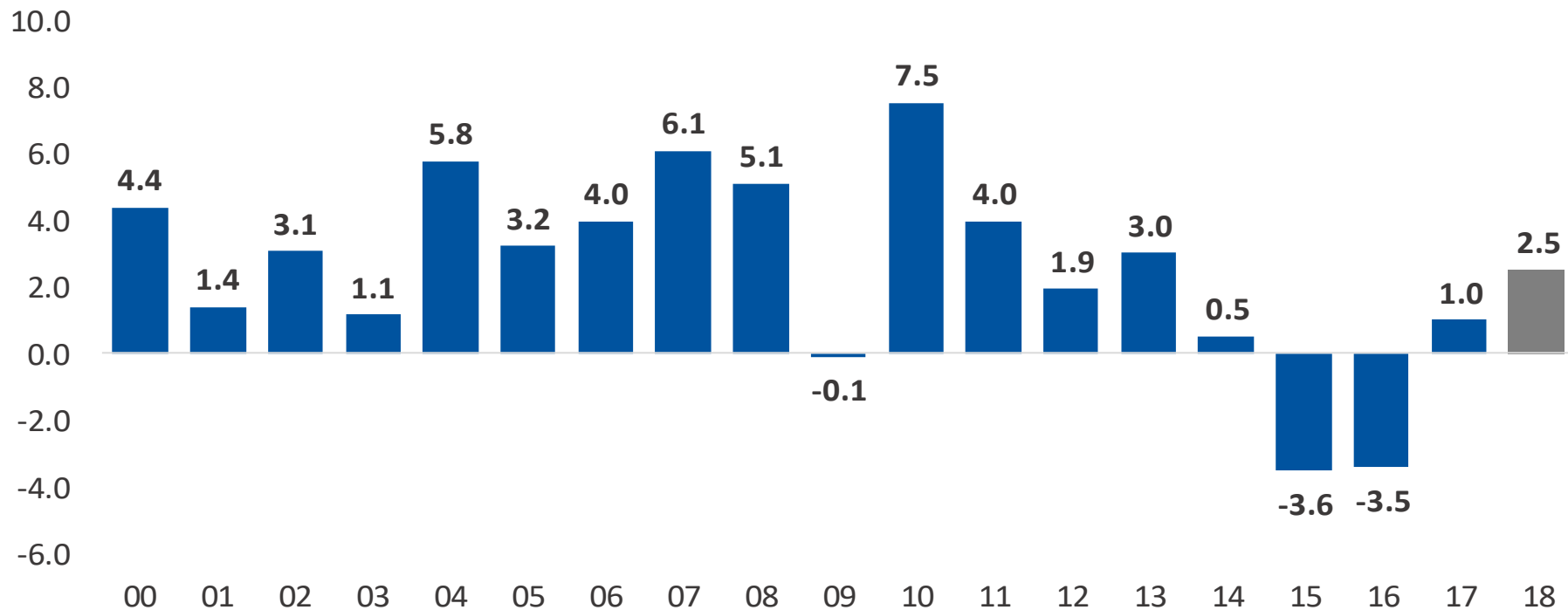
Monthly data, seasonally adjusted, at last month's price, in R\$ million



Source: BCB, Bradesco

# ANNUAL GDP

In 2018, economy will run close to potential



Source: BCB, Bradesco

But this is the **slowest pace**  
of recovery in more than **20**  
**years...**

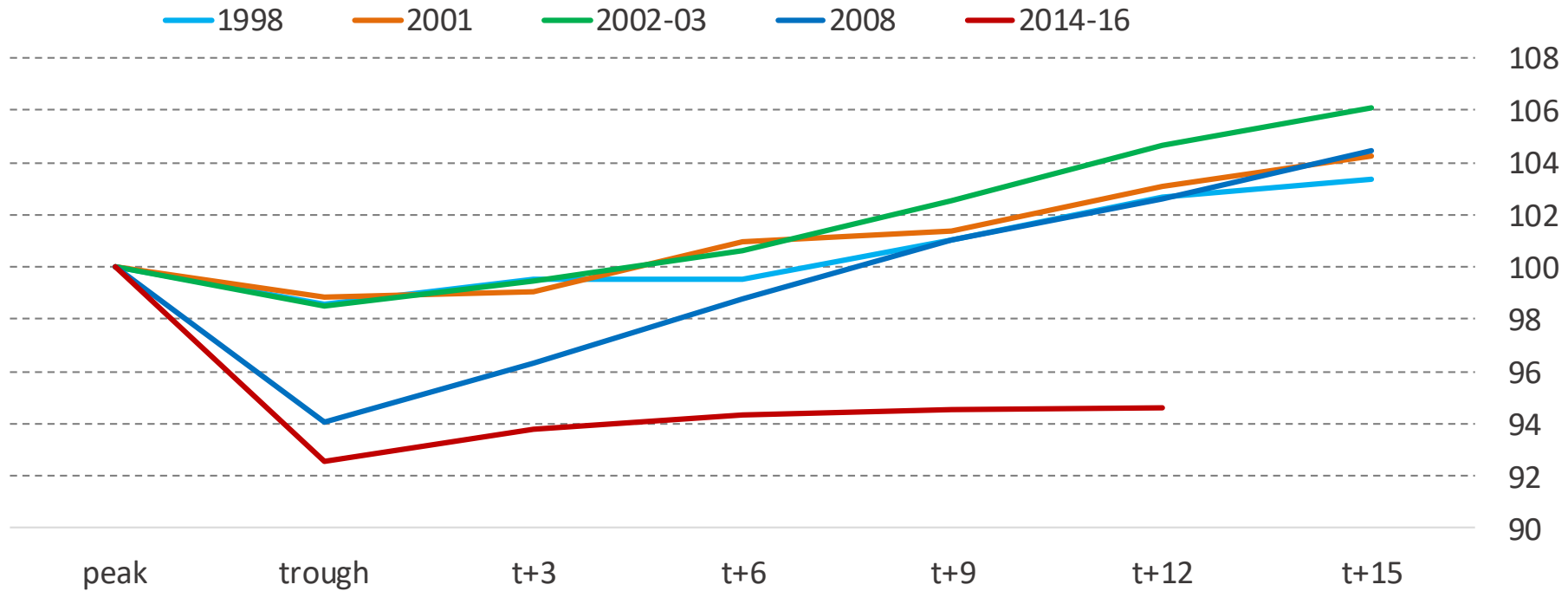


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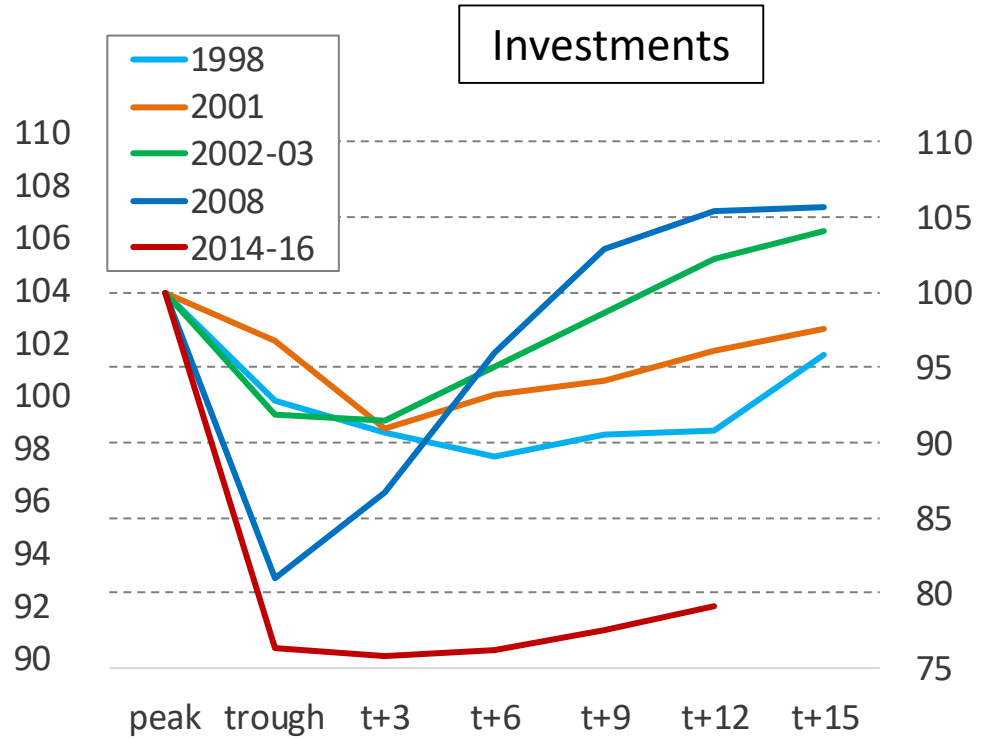
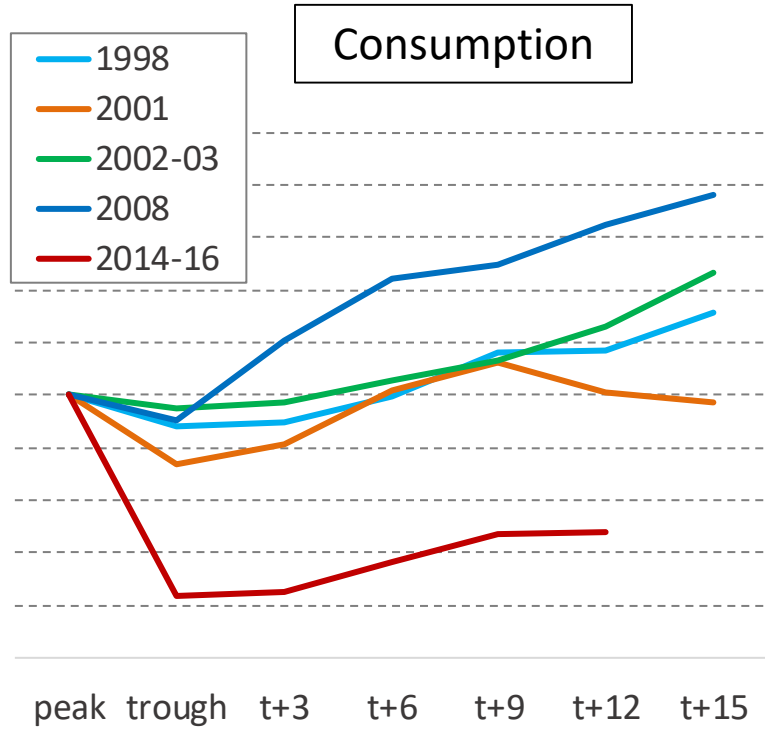
# CRISIS AND ECONOMIC RECOVERIES' EPISODES

GDP, 100 = pre-crisis peak



# CRISIS AND ECONOMIC RECOVERIES' EPISODES

GDP components, 100 = pre-crisis peak



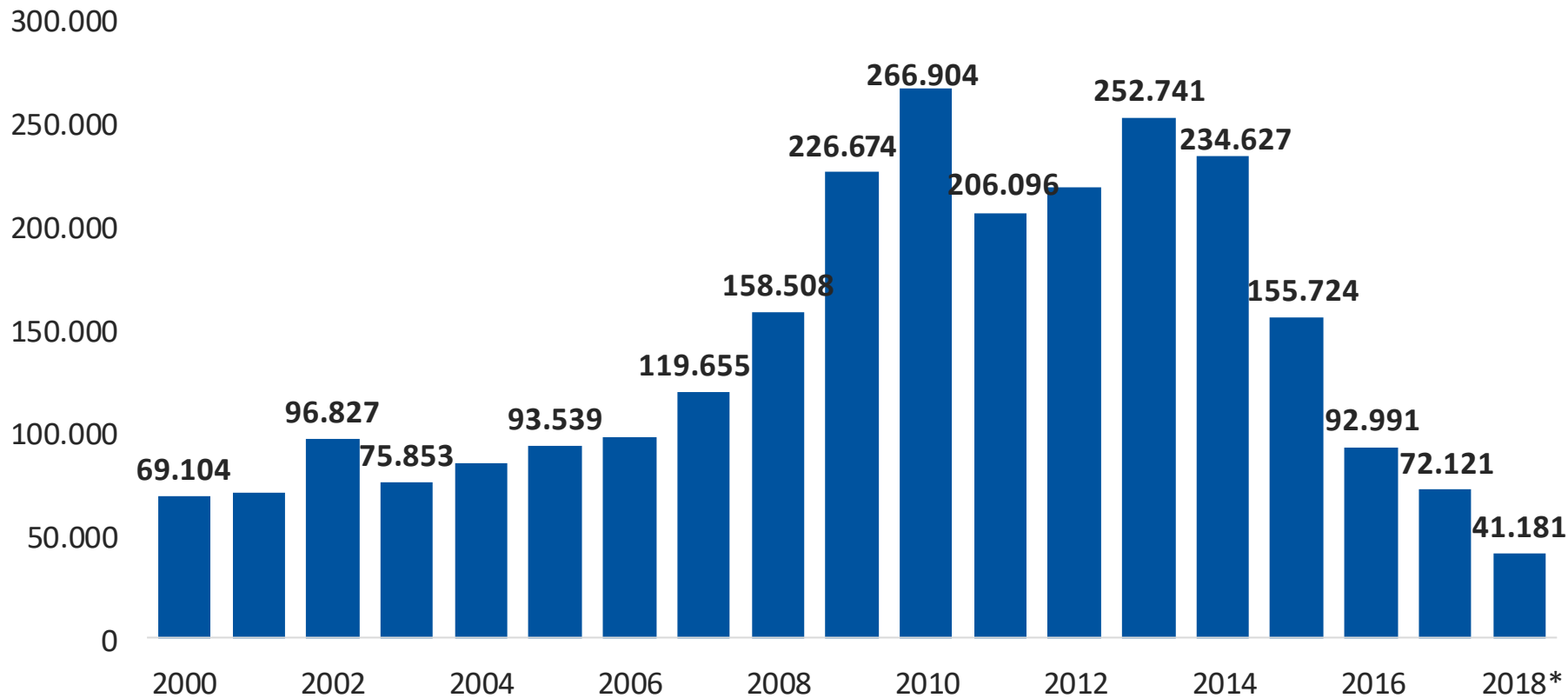
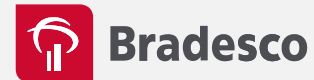
# WHAT LIES BEHIND THIS FRUSTRATING RECOVERY PACE?

## Main hypothesis

- **“Digestion”** of the **credit** problems during 2014-2017
- **Fiscal challenges**
- **Idleness** of the economy
- **Lack of investment capacity** from Federal Government, states and municipalities.

# BNDES LENDING

Annual, constant prices, R\$ mn

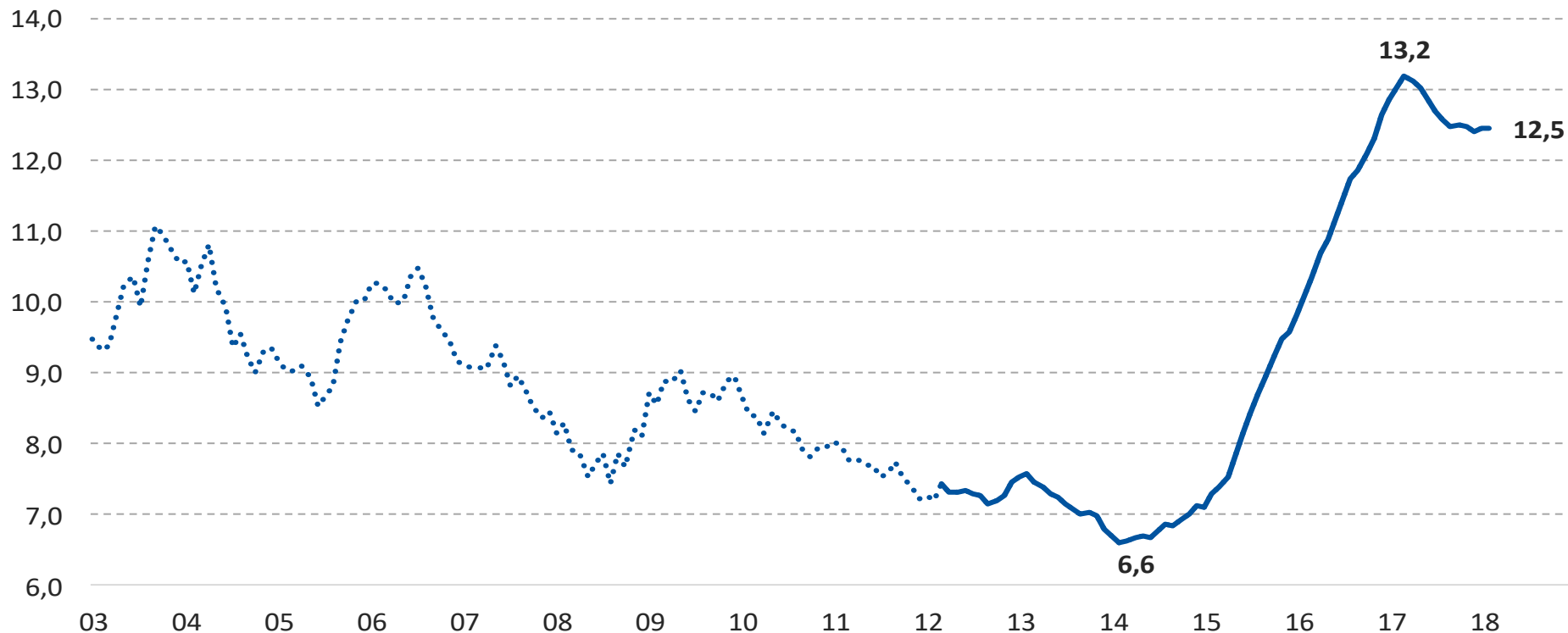
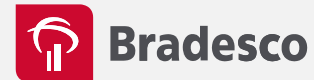


Source: BNDES



# UNEMPLOYMENT RATE

PNAD, %



Source: IBGE, Bradesco

That's why the **reform agenda** needs to **move forward...**



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# SUSTAINABLE GROWTH DEPENDS ON...

Main factors...

- **Growing investments** (including education)
- **Addressing the fiscal deficit**

# GDP PER CAPITA

2016, PPP



Bradesco

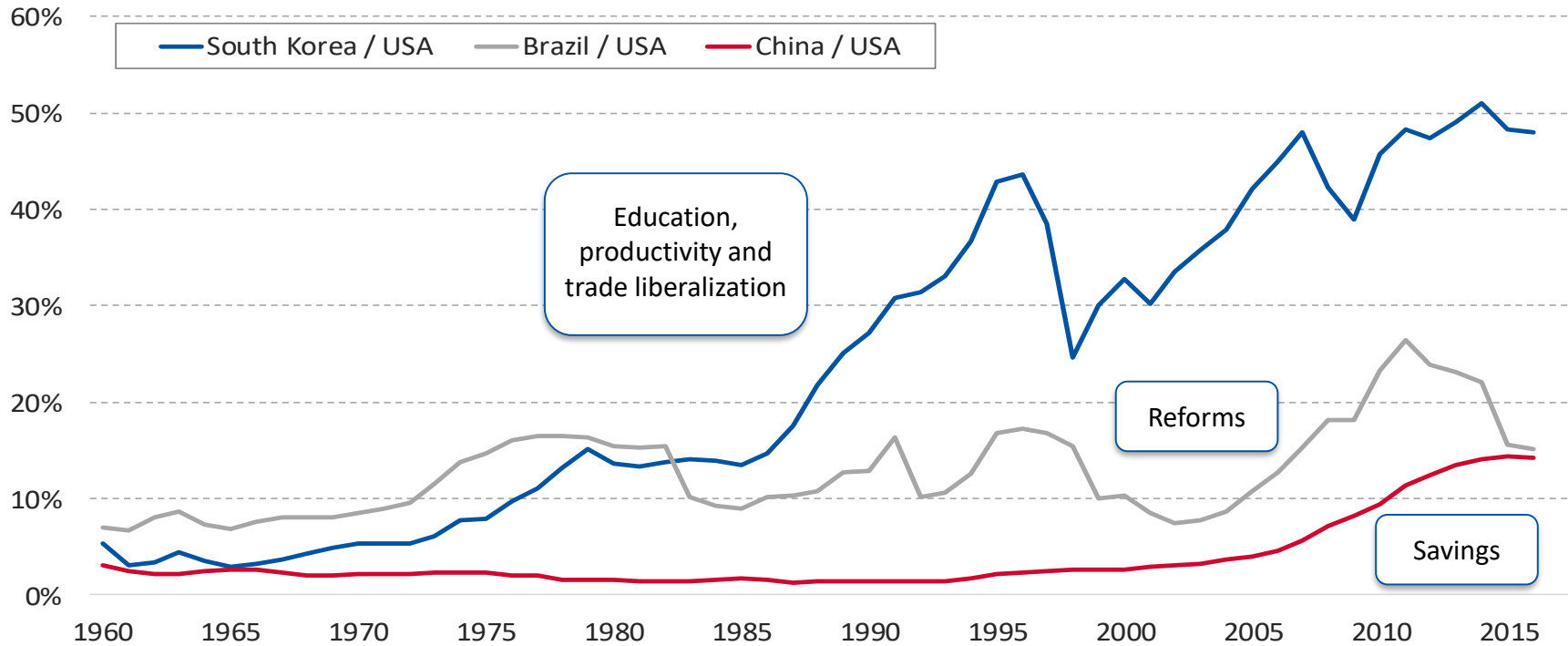
Latin America	
Chile	23,969
Uruguay	21,570
Argentina	20,171
Mexico	18,865
<b>Brazil</b>	<b>15,211</b>
Colombia	14,162
Peru	13,019
Bolívia	7,191

Developed Countries	
US	57,294
Australia	48,806
Canada	46,240
Japan	38,894
Korea	37,948
Spain	36,451
Italy	36,313
Portugal	28,515
<b>Brazil</b>	<b>15,211</b>

Peers	
New Zealand	37,108
Czech Rep.	33,223
Poland	27,715
Hungary	27,211
Russia	26,109
Turkey	21,147
Bulgaria	20,116
Thailand	16,835
China	15,424
<b>Brazil</b>	<b>15,211</b>
South Africa	13,179
India	6,658

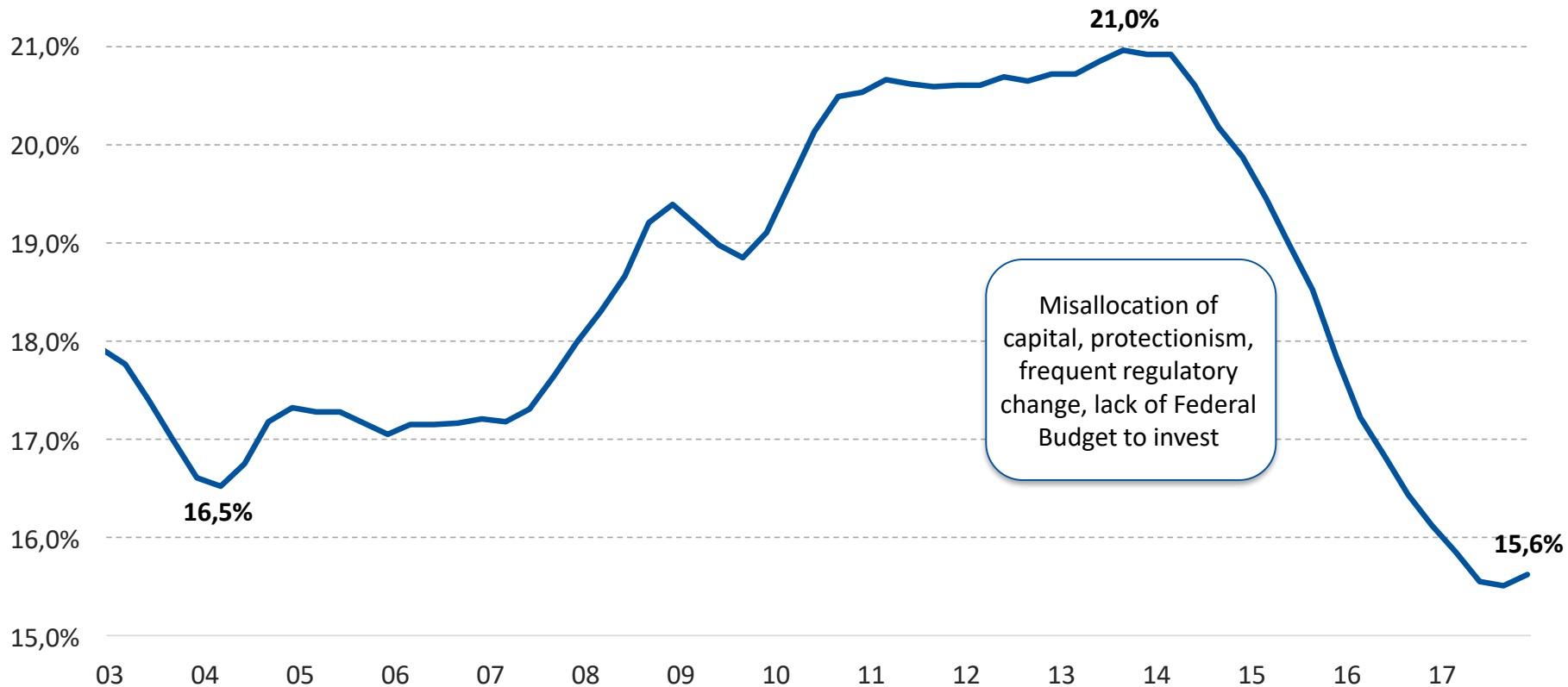
# PER CAPITA INCOME

Share of USA income, %



# INVESTMENTS

% of GDP

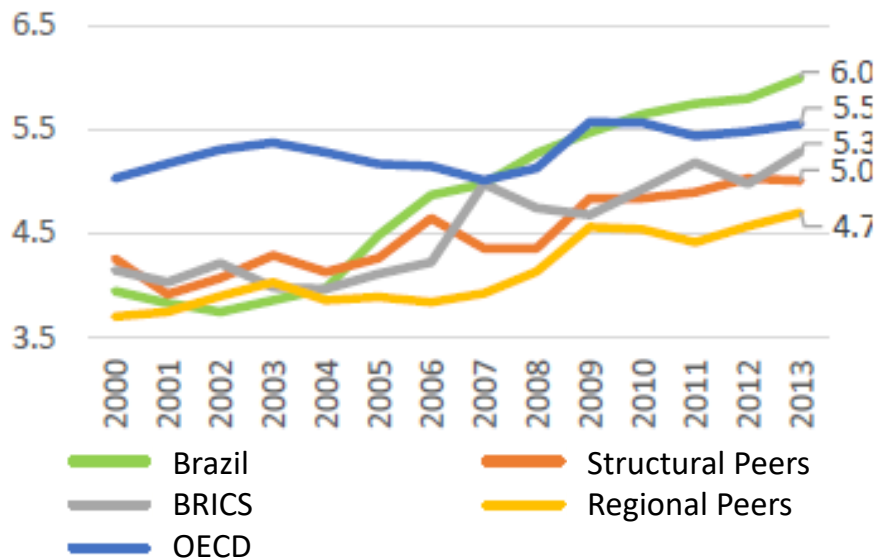


Sources: IBGE, Bradesco

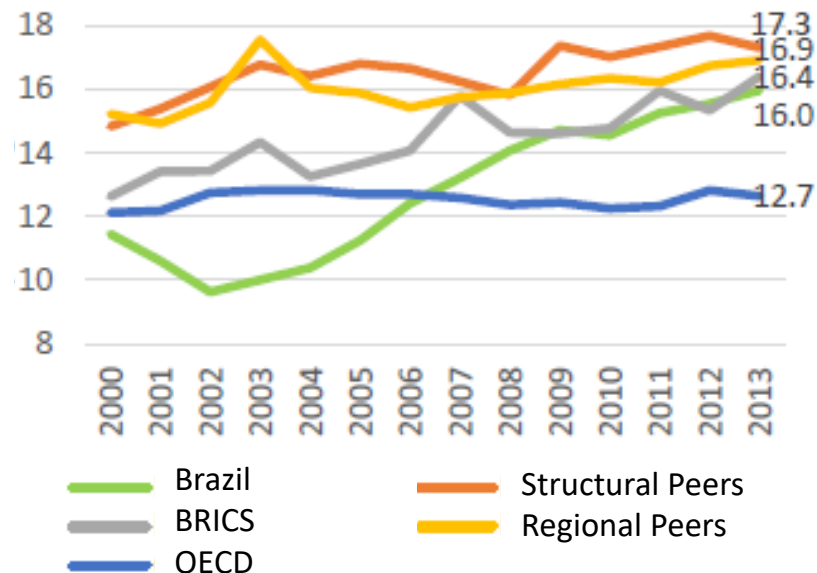
# PUBLIC EXPENDITURES ON EDUCATION

International comparison

### Education expenditures (% of GDP)

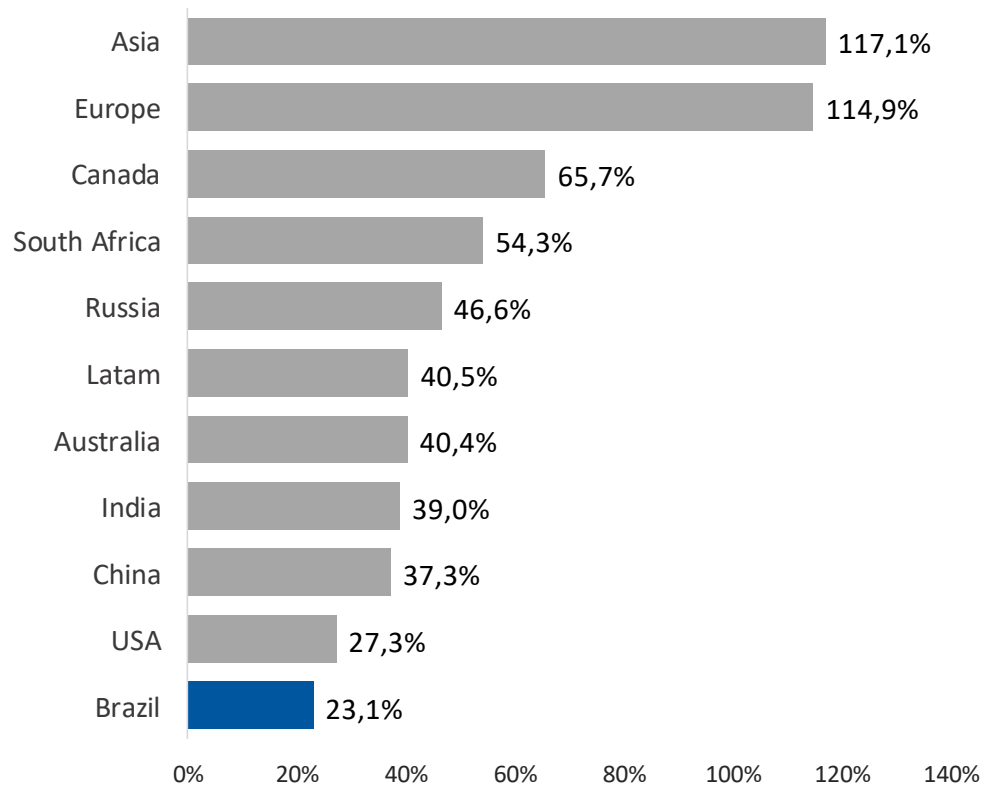


### Education expenditures (% of total public spending)



# TRADE OPENNESS

Exports + Imports (% GDP), 2017

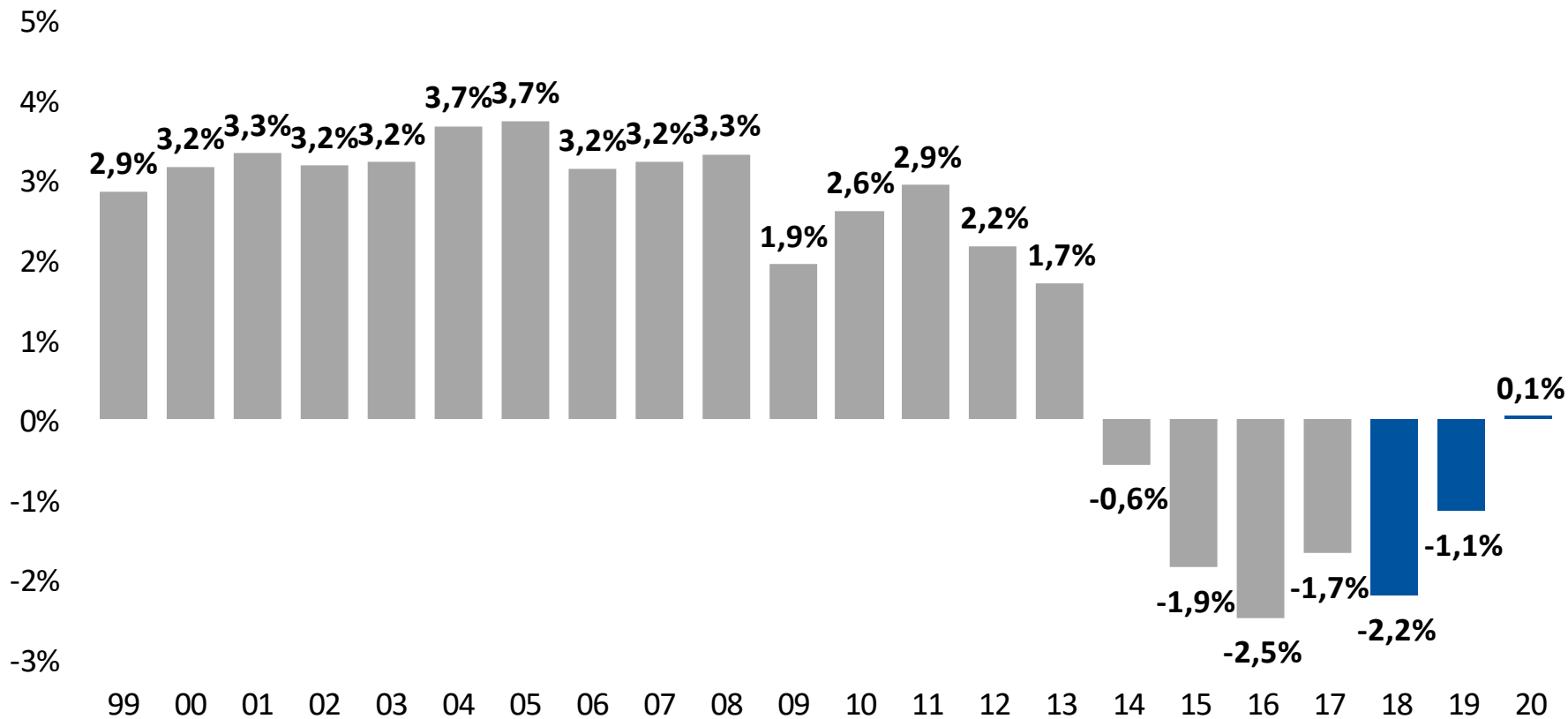


Source: EIU, Bradesco



# PRIMARY BUDGET

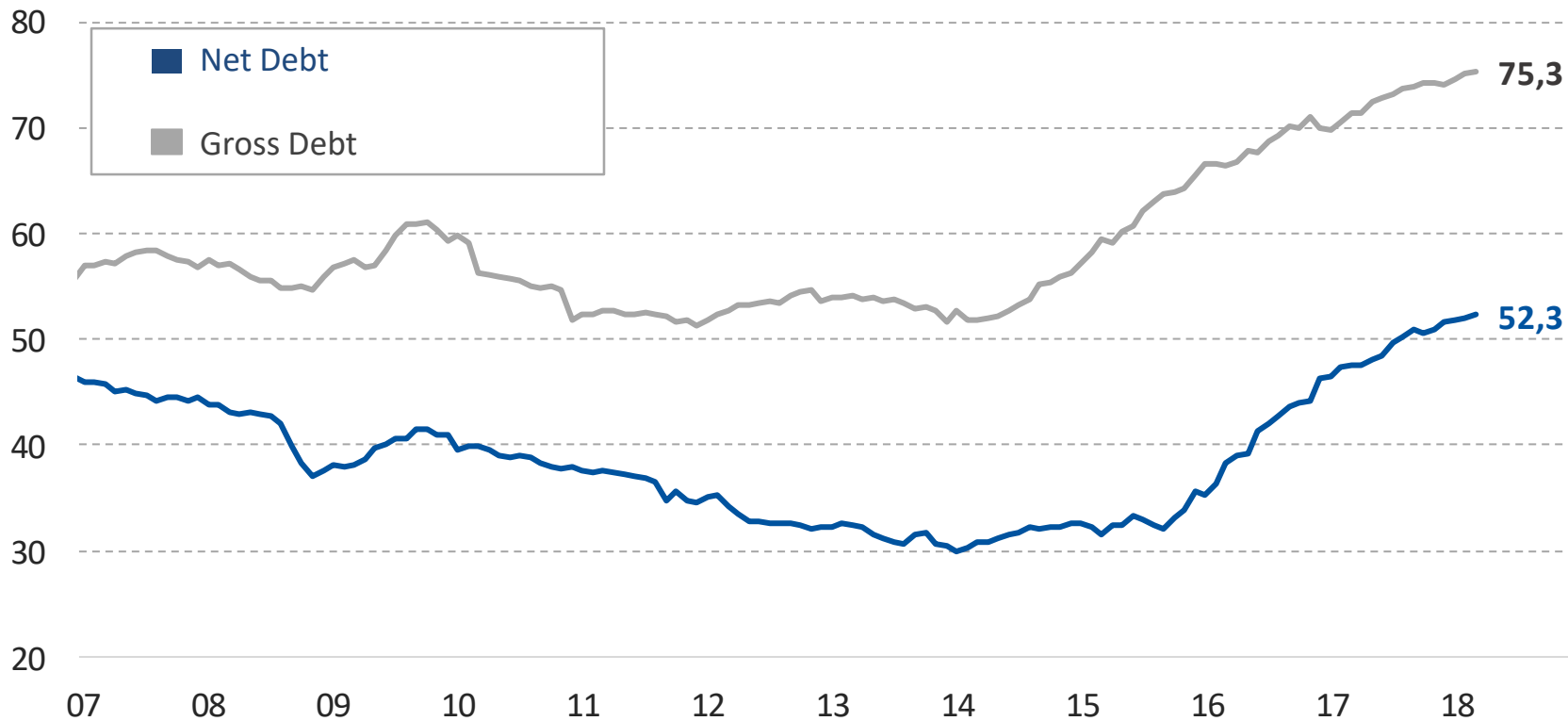
% of GDP



Source: BCB, Bradesco

# GROSS AND NET PUBLIC SECTOR DEBT

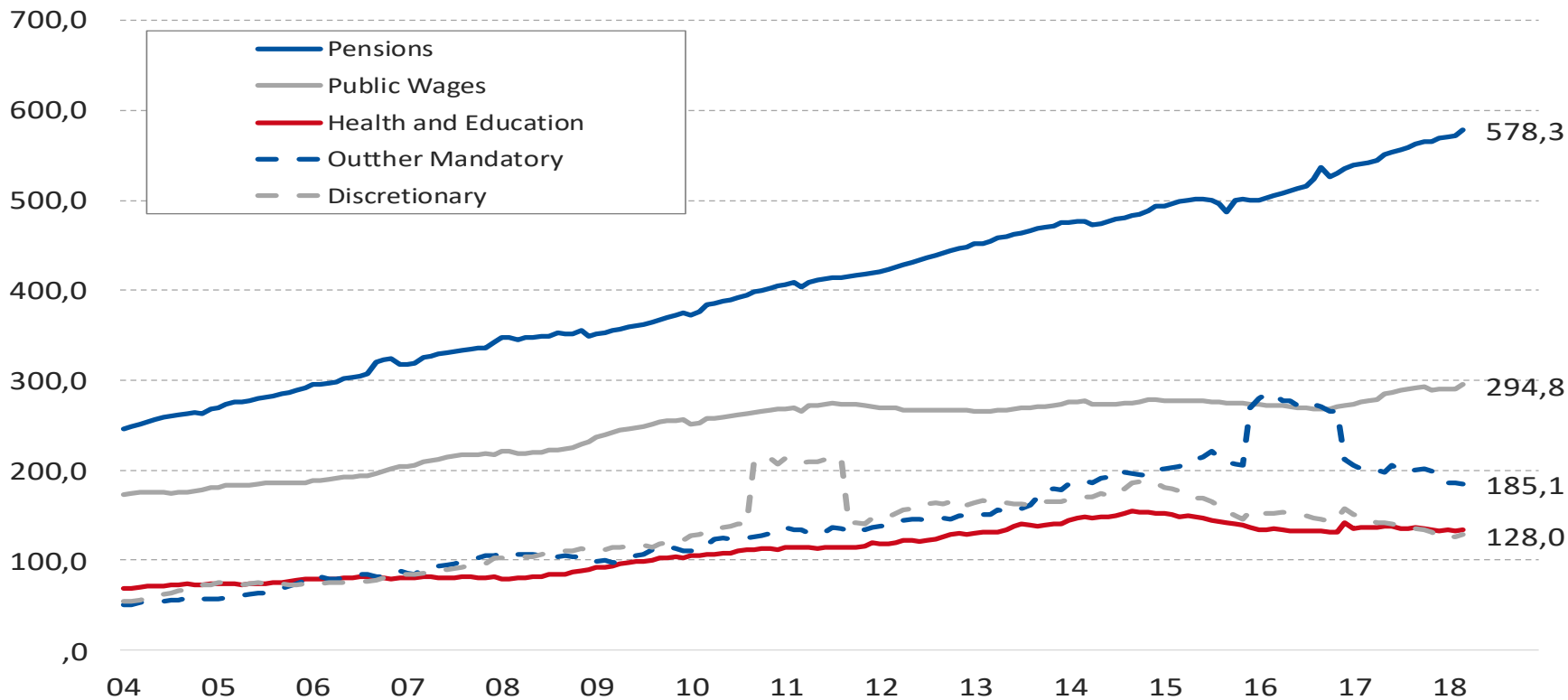
% GDP



Source: BCB, Bradesco

# FEDERAL GOVERNMENT EXPENDITURES

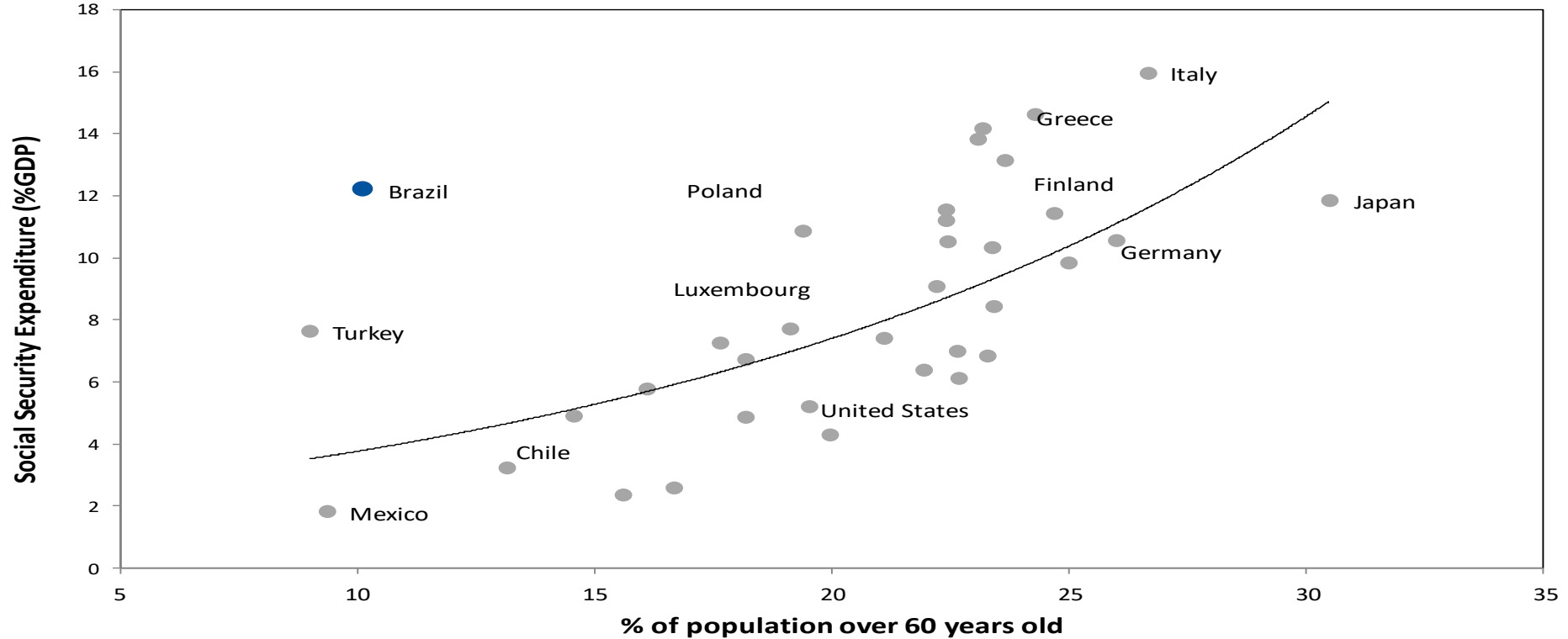
R\$ billion, constant prices



Fonte: Tesouro Nacional, Bradesco

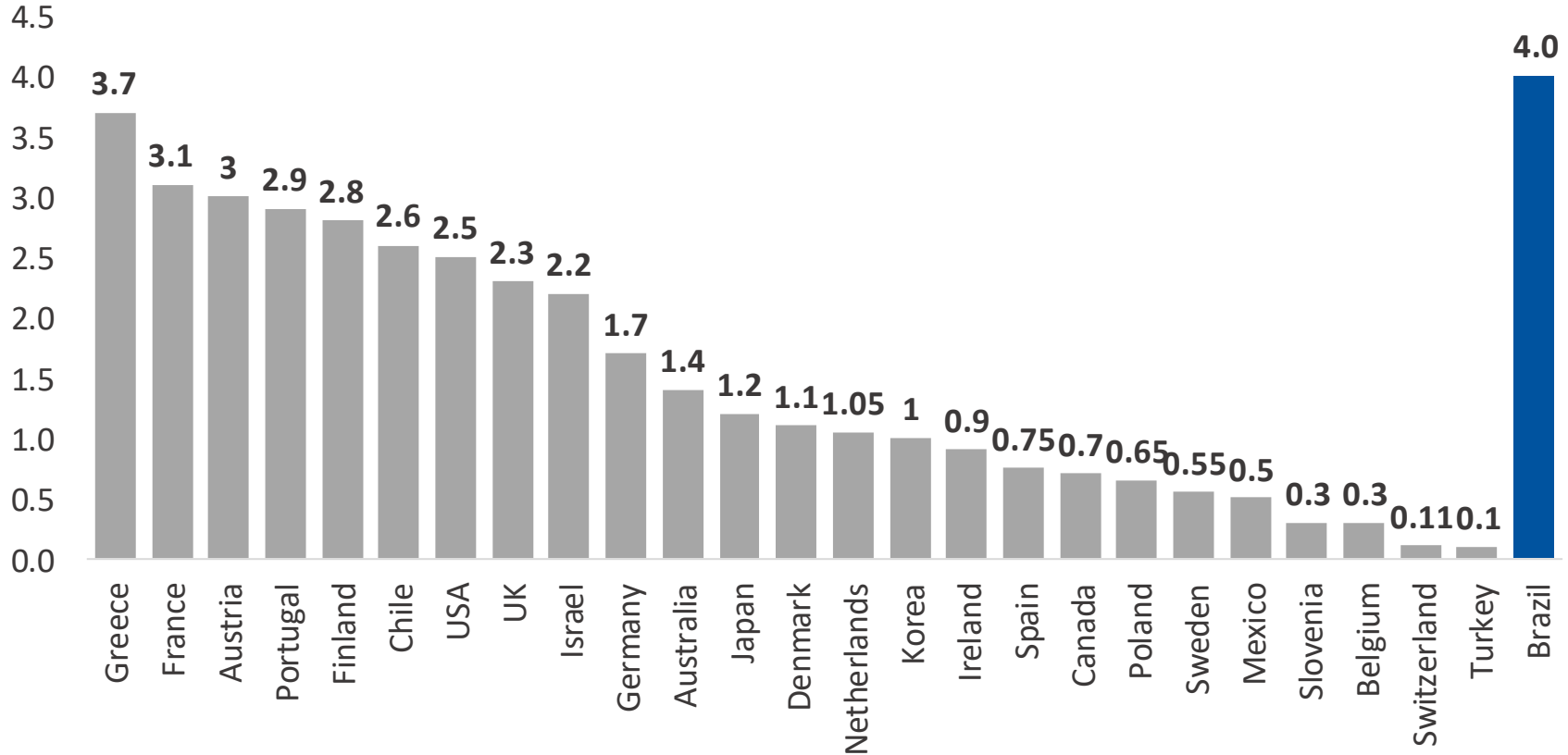
# SOCIAL SECURITY AND DEMOGRAPHY

As % of GDP; as % of elderly population



# PUBLIC SECTOR EMPLOYEES PENSIONS

% of GDP



Source: World Bank

If Brazil attacks this  
challenges, **long –term**  
**rates will converge** to peers  
and we'll **become**  
**investment grade again**



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# REAL INTEREST RATES

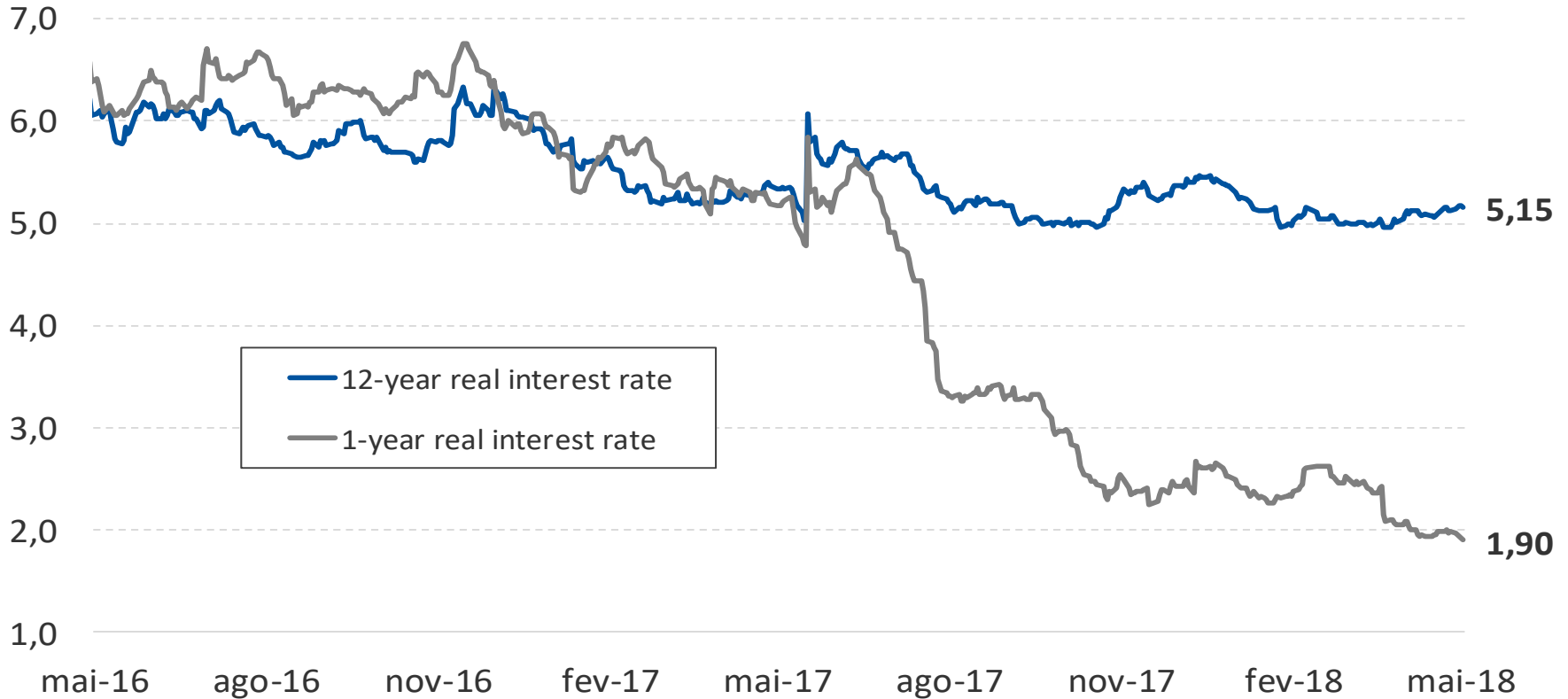
Selected countries

Countries	Real interest rate (ex-ante)
Turkey	7,3%
Russia	4,6%
Peru	3,4%
Mexico	3,3%
Argentina	3,0%
India	2,9%
Indonesia	2,4%
Brazil	2,4%

Countries	Real interest rate (ex-ante)
South Africa	1,8%
China	0,9%
Colombia	0,9%
Chile	0,4%
USA	0,1%
Poland	-0,2%
Japan	-1,0%
United Kingdom	-1,6%

# REAL INTEREST RATE

NTN-B, in %



Source: Ambima, Bradesco



	Sample mean	Investment grade		Speculative grade	
		AAA to A-mean	BBB+ to BBB-mean	Speculative grade mean	Brazil
<b>Total external debt / GDP</b>	52%	67%	50%	45%	27%
<b>Net external liabilities / GDP</b>	19%	-11%	34%	55%	36%
<b>International Reserves (US\$ bi)</b>	138	226	93	45	377
<b>International Reserves (months of import)</b>	8,6	8,0	8,2	9,1	30,0
<b>Current account / GDP (*)</b>	-3,3%	-1,5%	-2,6%	-4,2%	-0,3%
<b>External financing needs / (Reserves + Exports) (**)</b>	150%	197%	114%	132%	62%

Sample from 70 countries

\* Mean of deficit countries

\*\* Current account + Debt servicing maturing in 12 months

Source: EIU, S&P, Bradesco

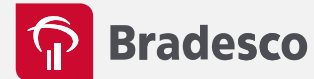
# What is happening to the **Brazilian** exchange rate?



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# EXCHANGE RATE

R\$/US\$



Source: Bloomberg, Bradesco

### Global:

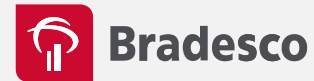
- Increased volatility
- Rising interest rates
- Protectionist measures
- Contagion from Argentina

### Local:

- Slow pace of economic recovery
- Interrupted Fiscal Agenda
- Lowest interest rates differential in history

# INTEREST RATES DIFFERENTIAL

Brazil vs peers, 1 year rate

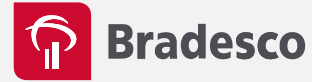


Source: Bloomberg, Bradesco

Countries: South Africa, Turkey, Russia, Chile, Colombia, Peru, Mexico e Australia

# SHOULD WE BE CONCERNED ABOUT THE DEVALUATION?

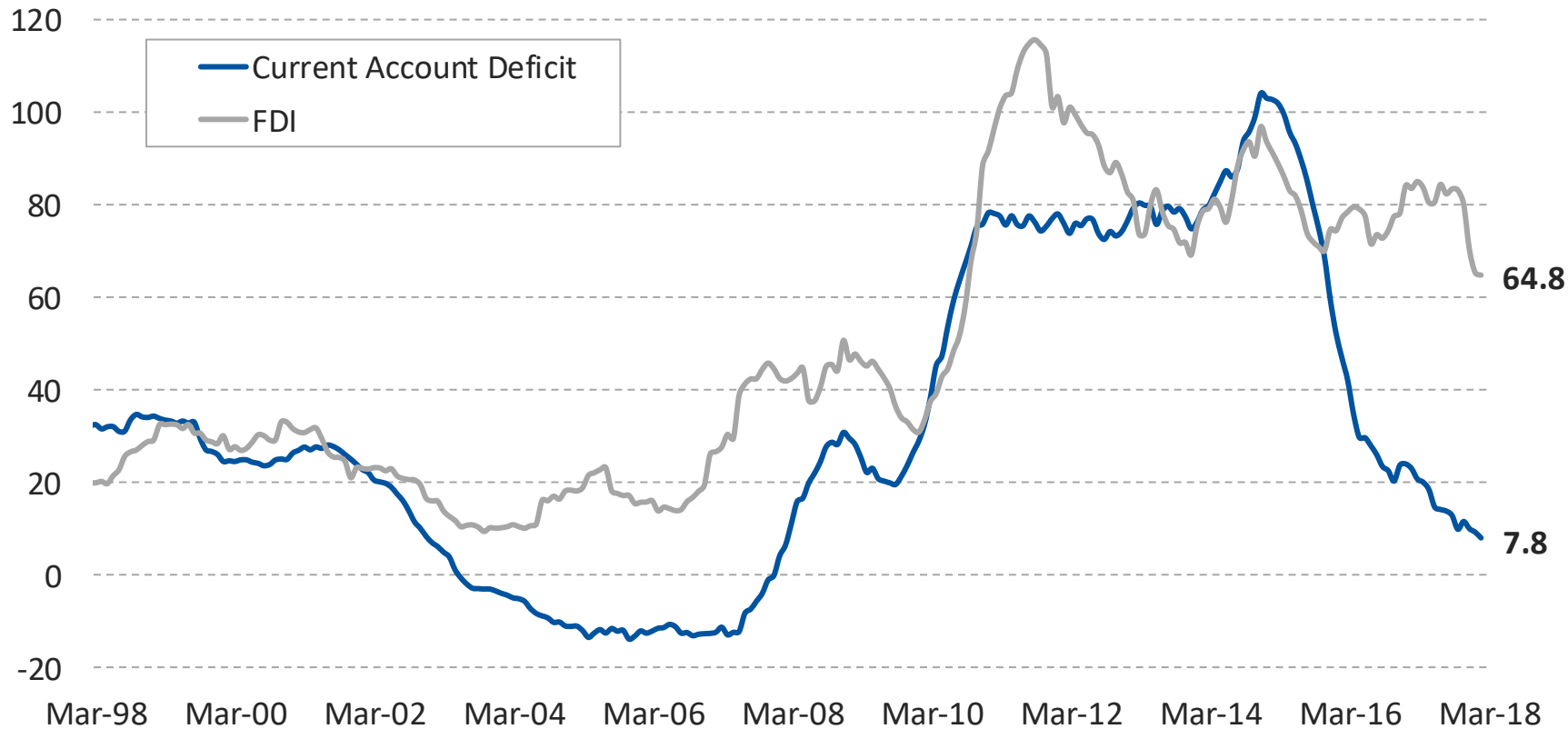
## Main Points



- Low inflation. Even with the BRL at 3,60-3,70 inflation remains on target
- Foreign holdings of local debt at a 6 year-low
- Lowest external deficit in 10 years (0,4% of GDP)
- Reserves (US\$ 380 billions) and exchange rate swaps at comfortable levels
- Government (\$ 70 billion) and SOE's external debt (\$ 100 billion) at low levels

# CURRENT ACCOUNT AND FDI

USD Billions, 12 months



Source: IBGE, Bradesco

# REAL EFFECTIVE EXCHANGE RATE

Jun/94 = 100



Source: Bloomberg, BCB, Bradesco



# Elections



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	Sep-17	Nov-17	Apr-18
Lula (PT)	18	17	13
Jair Bolsonaro (PSL)	9	11	11
João Dória (PSDB)	1		
Marina Silva (REDE)	1	1	1
Geraldo Alckmin (PSDB)	-	1	1
Ciro Gomes (PDT)	1	1	1
Alvaro Dias (Podemos)	0	1	1
Dilma (PT)	-	-	-
Michel Temer (PMDB)	-	1	-
Joaquim Barbosa (PSB)	0	0	1
Other Answers	3	2	4
Null	18	19	21
Don't Know	48	46	46

### Key dates:

**June-July** – Political parties plenaries

**Aug, 15<sup>th</sup>** – Registering

**Aug, 31<sup>st</sup>** – TV Campaign

**Sep, 17<sup>th</sup>** – TSE rules on candidates

**Oct, 7<sup>th</sup>** – 1st. Round

**Oct, 28<sup>th</sup>** – 2nd. Round

	2017	2018	2019
Consumer inflation - IPCA (%)	3,0	3,5	4,3
GDP growth (%)	1,1	2,5	3,0
Industrial Production (%)	1,4	3,5	3,0
Retail Sales (%)	1,5	3,0	4,5
Unemployment Rate (% of labor force)	12,7	12,1	11,8
Outstanding Credit Growth (%)	1,0	4,5	8,3
Trade Balance (BCB, USD bn)	64,0	67,0	61,1
Current Account (USD bn)	-7,2	-15,7	-37,8
Exchange Rate (BRL/USD, eop)	3,25	3,35	3,45
Selic (% eop)	7,00	6,25	8,00
Primary Balance (BRL bn)	-159,0	-154,0	-88,0
Gross Debt (% of GDP)	74,0	75,0	76,5

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