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A SUMMARY OF THE RECENT MACROECONOMIC SCENARIO

To kick off 2023, I gathered a handful of macroeconomic indicators on Brazil. And what a better time than now considering the new economic model presented by the new president's team. To facilitate the analyses, all indicators use the same timeframe: the last 10 years.

The first indicator shows Country Risk behavior (Figure 1). From the perspective of investors (foreigners mainly), the risk peak occurred at the turn of 2015 and 2016. In the last 3 years, tensions were more stable, although the 2019 health crisis led to higher risk levels. In turn, the Exchange Rate (Figure 2) saw a strong devaluation trajectory of the Brazilian Real throughout the selected period, with emphasis on the moment when production stopped during the health crisis. Since then, the exchange rate in the BRL5.00 and BRL5.50 range has been the currency's reality.

Macroeconomic forecasts for the next years by government, investment managers and large banks are for the risk rate to increase in several world economies (including Brazil), with the constant presence of weak indicators by the world's largest economies (which point to an imminent recession) and general panorama of public policies that the country will adopt. These factors will force Brazil's currency to continue its devaluation path, easily surpassing the BRL6.00 barrier in 2023.

Figure 3 shows the Selic rate's trajectory in the last 10 years. We clearly see the indicator rising to levels close to 2015, the peak of Brazil's last financial crisis. With effects on the entire economy, the Central Bank is expected to maintain the Selic Rate (benchmark for interest rates on loans and investments) in double digits for at least the next 3 years.

Figure 4 shows the evolution in Brazil's Trade Balance. Since 2014, the country has registered annual surpluses, although we did see a drop between 2017 and 2019. For

Figure 1 – Country Risk – Brazil

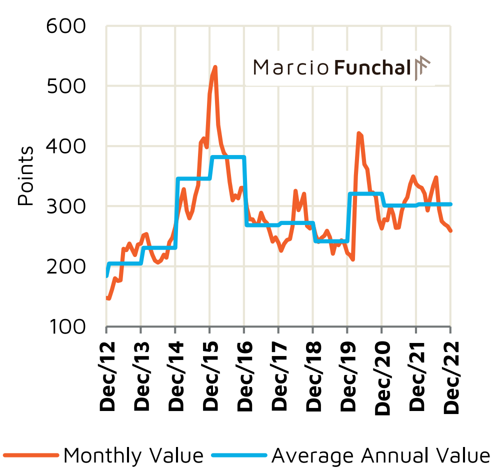

Figure 2 – Exchange Rate – U.S. Dollar

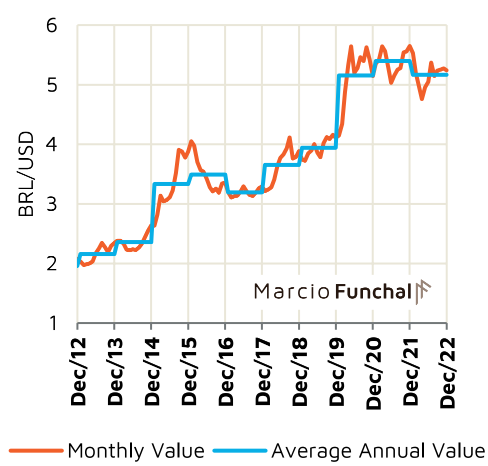

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Figure 3 – Selic Rate

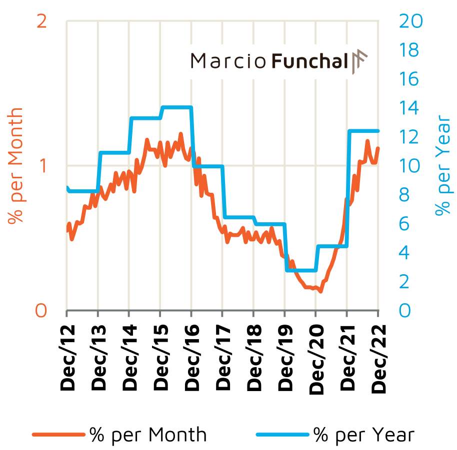
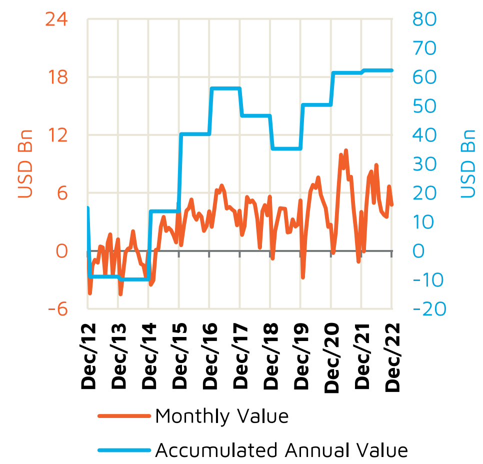


Figure 4 – Brazilian Trade Balance



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the next few years, agents expect the annual growth rate to continue, taking advantage of spaces already conquered in international markets.

The evolution in GDP growth is shown in Figure 5. We see that, in the last 10 years, GDP shrank in 3 of them, but in a significant level (retractions of more than 3.5% per year). In the periods of positive growth, only 2021 posted an annual rate greater than 4%. Analysts project an average annual growth (nominal) of 0.5% to 1.5% for the next years.

With regards to Industrial Production, Figure 6 shows a dramatic trajectory, as current levels represent a retraction of roughly 15% in relation to 10 years ago. Despite this, the country has maintained a stable production level since 2015, with a sharper drop in 2020, due to the economic shutdowns imposed by the State. Specialist projections for this indicator are not optimistic, as they range from slightly negative annual growth to, on the opposite side, small annual increases (less than 2%). Thus, in averaging out the different views, production levels are expected to remain as is in the short term.

The Retail Sector's evolution is presented in Figure 7. The seasonal effect of the year-end is clearly visible, as are the effects caused by stoppages during the pandemic in 2020. In summary, current sales saw little growth in the last 10

Figure 5 – GDP Growth Rate

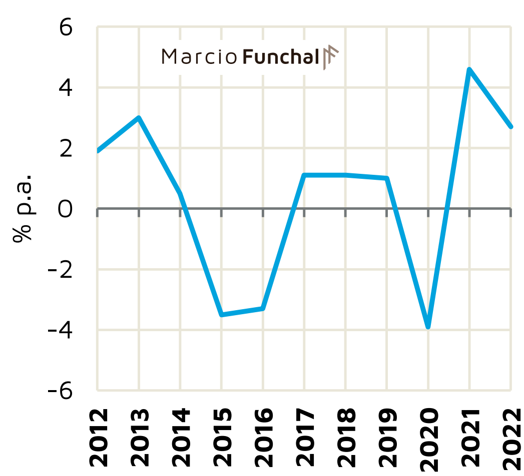

Figure 6 – Industrial Production Growth Rate

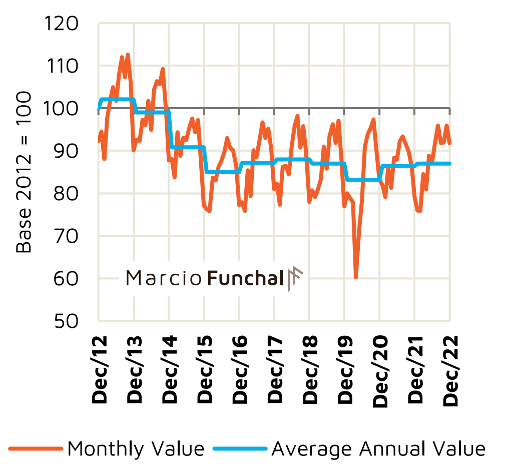

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Figure 7 – Variation in Retail Trade Sales in Brazil

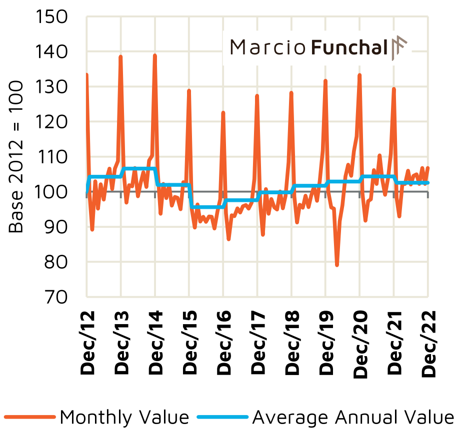
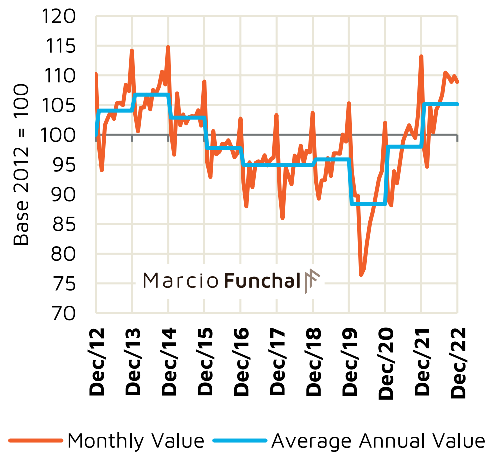


Figure 8 – Growth Rate of the Services Sector in Brazil



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years (less than 3% in the accumulated), despite the strong increase in online sales and stronger distribution channels. In the short term, analysts predict this indicator will remain stable, with the possibility of small annual increases (no more than 2%).

Figure 8 presents the Services Sector's sales-volume evolution. The data shows the sector growing as of 2017, despite the impacts of the economy shutdown during the 2020 Covid pandemic. However, over these 10 years, service sales are only 5% higher today than at the beginning of the period. As in the case with the Industrial and Retail sectors, macroeconomic projections by government, investment managers and large banks for the Services Sector point to small annual growth for the sector in the short term (around 2% and 5% per year).

In terms of Unemployment, Figure 9 shows rapid growth between 2012 and 2019, replaced by a sharp decline at the end of the selected period. Unemployment projections for the next three years diverge significantly among analysts, but hover between 8 and 11% per year.

Figure 10 shows that public accounts worsened significantly in recent years, particularly after 2013 when

Figure 9 – Unemployment

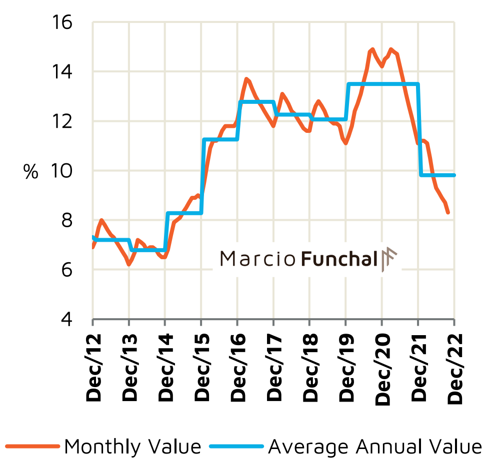

Figure 10 – Public Accounts

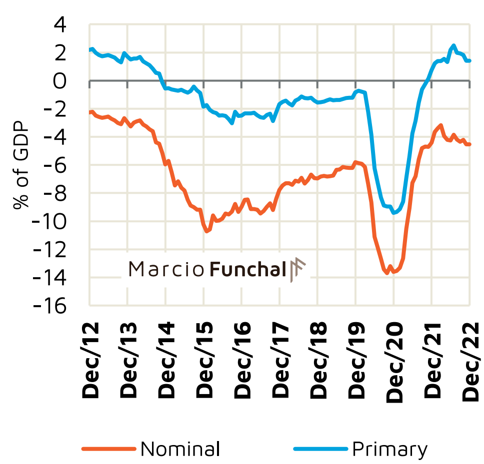

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Figure 11 – Brazil's Public Debt

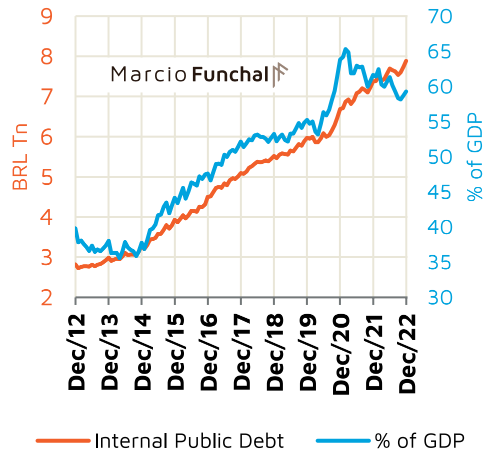
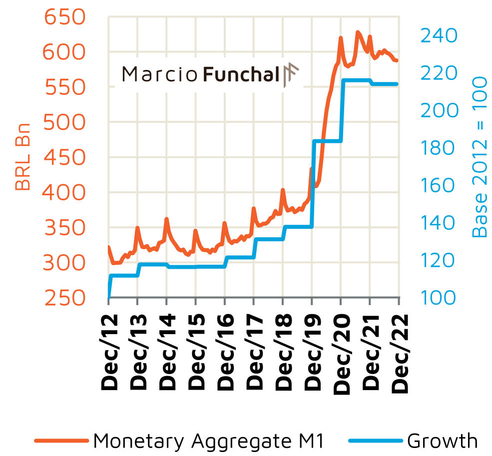


Figure 12 – Monetary Aggregate M1



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the country stopped registering a primary surplus (balance of public accounts before debt interest payments), which means that the government spent more than it collected for several years. 2020 was a record-breaking year, due to public spending with the health crisis. This spending scenario was only reversed in 2022, when government accounts started to show a positive balance again. However, analyst forecasts are unanimous in pointing to the return of unbridled public spending since the new government's economic plan has already announced that it will not meet surplus targets. In the short term, the deficit is expected to return to 2015 and 2016 levels of around 2% of GDP per year.

Still regarding the country's indebtedness, Figure 11 shows that in the last 10 years there has been a strong growth in Brazil's securities debt (securities and bonds issued by the Federal Government and the Central Bank). Today, this debt component alone is equivalent to around 60% of GDP. Analysts project that, with the recent measures to exceed the spending limit and flexibilization of fiscal austerity, Brazil's securities debt will quickly reach levels close to 80% of GDP in the coming years.

Lastly, Figure 12 summarizes the growth of "money" in circulation in Brazil (Monetary Aggregate M1 is the total currency in circulation in the economy that is not related to investments, represented by the bank balance at the Central Bank and other agents of the official banking system). This rapid growth is explained by the constant "printing" of money by the Central Bank, as a way of honoring its payment obligations. It is important to highlight that the State only has three basic forms of capitalization: (a) increase tax collections, (b) contract more debts or loans (through securities debt, for example) or (c) issue more money. All these actions, individually or together, reduce the official currency's purchasing power, thus causing currency inflation (which is mistakenly understood as price increases). According to the specialists consulted, the rapid growth of M1 is expected to continue in the short term.

Considering the indicators presented, it is easy to see that the country's economy will be under strong pressure in the next 2 to 3 years, with the business sector facing major challenges. Thus, it is highly recommended that companies review their business scenarios and strengthen their long- and short-term strategies. ■