BANK OF COMMUNICATIONS BBM

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Materialization of Risks

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The first month of 2020 was marked by important shocks to the global economy, that increase the risks surrounding the expected recovery to global output in the year. The Australia fires, tensions in the Middle East, and the Coronavirus outbreak in China augment the chance of a loss of momentum in global activity, which has figured as one of the main negative risks in our scenario.

The industrial PMIs of December and January showed a consolidation in the moderate recovery trend already suggested in most countries. This improvement happened despite an unexpected geopolitical shock in the first week of the month: the rise in political tensions between the US and Iran, after an Iranian general was killed by American forces. After an exchange of verbal threats between the two nations and a rise of almost 5% in oil prices, the situation cooled down throughout the month, along with the price for the commodity. But the region will probably remain as a source of concern throughout the year, reflecting the delicate state of the Iranian regime. On the other hand, the Coronavirus outbreak that started in China over the second half of January remains a source of concern and its consequences are ongoing as we enter February. Not only did the virus infect over 24 thousand people and killed almost 500 in China alone, the outbreak also hit the Chinese economy at a very sensitive economic time: the Lunar New Year holiday. The New Year holiday is a particularly important time from an economic point of view, with a high volume of travel undertaken inside the country, and strong retail and services activities, reflecting the festivities and the reunion of families that mark the extended holiday.

The Chinese Government acted fast in order to control the outbreak. Sixteen cities in the Hubei province, which is the epicenter for the epidemic, were put in lock down, public festivities were canceled, and the holiday extended for two days. Many localities still recommend that workers remain at home and delay their return to work. Therefore, the negative effects over the economy will probably be sizable due to the interruptions in plans and activities, which has led to a wave of downward revisions to growth over the first quarter and the year. With the current information, Chinese growth is expected to be close to 5.5% in 2020, downgraded from 5.8%. The duration of the epidemic and of the disruptions to activity will determine the extent of the revisions to growth over the next few weeks.

In Brazil, the beginning of the year has been benign. Despite some frustration with the industrial data for end-2019, the incoming economic data remain in line with our expectation for moderate growth in 2020, driven by the pick-up in consumer spending and investment growth. Consumer credit growth remains strong, and the labor market shows a gradual improvement. The declines in meat and gas prices brought some relief for inflation for the first quarter, and we revised downwards our forecast for the year-end CPI to 3.5%. Therefore, we maintain our scenario of a

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steady Selic rate at 4.25% until the last quarter, when the Central Bank might begin a normalization cycle of the interest rate.

With the return of the work in Congress, we will continue to monitor carefully the reform agenda being appreciated by the legislative body. In our point of view, the “Emergency” Constitutional Amendment in the Senate (which is compatible with Amendment 438 currently being considered by the House), should be the priority for the first semester, since its approval would enable a more efficient management of public expenditure. It could also serve as a trigger to upgrades to the ratings of the Brazilian sovereign debt throughout the year.

ECONOMIC FORECASTS	2014	2015	2016	2017	2018	2019	2020F	2021F
GDP Growth (%)	0,5%	-3,5%	-3,3%	1,3%	1,3%	1,2%	2,1%	2,5%
Inflation (%)	6,4%	10,7%	6,3%	2,9%	3,7%	4,3%	3,5%	3,7%
Unemployment Rate, SA (%)	7,1%	9,6%	12,6%	12,4%	12,2%	11,7%	11,0%	10,7%
Policy Rate (%)	11,8%	14,3%	13,8%	7,0%	6,5%	4,5%	4,75%	6,5%
External Accounts								
Trade Balance (US$ bn)	-4	20	48	67	53	39	37	40
Current Account Balance (US$ bn)	-104	-59	-23	-10	-42	-51	-61	-60
Current Account Balance (% of GDP)	-4,3%	-3,3%	-1,3%	-0,7%	-2,2%	-2,8%	-3,2%	-2,5%
Fiscal Policy								
Fiscal Primary Balance (% of GDP)	-0,6%	-1,9%	-2,5%	-1,8%	-1,6%	-0,9%	-1,5%	-0,9%
Government Gross Debt (% of GDP)	57,2%	66,2%	69,4%	73,7%	77,2%	75,8%	77,0%	76,0%

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