

## Monthly Macro Letter

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# Mitigation Policies

**Fernanda Guardado**  
Chief Economist

**Serge de Valk**  
Economist

**Alvaro Borges**  
Intern

**Anna Saraiva**  
Intern

**Giovanni Machado**  
Intern

With the COVID-19 pandemic advancing throughout the globe, the uncertainty surrounding the economic prospects of the world remains huge. But one certainty seems to be consolidating: the negative economic impact of the shock, which is completely different from the shocks witnessed in the last century, will be deeper and larger than the ones experienced over the Great Financial Crisis of 2008. In this backdrop, the world economy seems to be entering a recession close to -1.5%, larger than the one witnessed in 2009.

An example of the speed and virulence of the economic effects of the epidemic can be seen in the rise of initial jobless claims in the US, which over the last couple of weeks of March reached almost 10 million new claims. Such level is unprecedented in claim's historical series, and points to a substantial increase in the unemployment rate over coming weeks. While mitigation and countercyclical policies have been announced by the American Government, the contractionary impact in the economy seems inevitable, and deep.

Several State governments in Brazil acted fast throughout the month and imposed restrictive measures to activity and personal interaction, in order to mitigate the spread of the epidemic. Big urban centers like São Paulo and Rio de Janeiro have on their hands the challenge of avoiding an overwhelmed health system, should there happen a large spike in the number of severe cases of the disease, requiring ICU and beds in numbers above of the current availability.

As the restrictions or lockdowns are extended in Brazil – several States have already announced that measures will be in place until at least mid-April - so are the economic effects being increasingly felt domestically. High frequency indicators suggest a drop of over 70% in activities related to durable goods retail and services, which are amongst the hardest hit sectors. Even once the restrictions are lifted, it is possible that some negative effects will continue to weigh temporarily on consumption and leisure preferences of the population, dragging down demand over the ensuing months.

Both the Central Bank of Brazil and the Ministry of Economy have announced a host of policies aimed at mitigating the effects, on the economy, of the fight against the virus. The measures announced by the BCB were aimed at promoting ample liquidity and guaranteeing the normal functioning of all parts of the credit market, especially the ones that were frozen due to the rise in risk aversion. These measures will be complemented by the power to the BCB to buy public and private bonds, which shall be approved soon by Congress with the new "War Budget" proposal. The Ministry of Economy has made available many programs and measures to support income and employment, but we would single out as the most relevant the labor flexibilization program, which allows companies to suspend labor contracts or to decrease wages and hours worked, with the Government making up for part of the worker's lost income. The program will last for 2 months. We believe this program has great potential to help small and medium enterprises cross the most dramatic period of demand decrease, through the cut in labor

costs, while still supporting the income of workers and maintaining work attachment. The rapid implementation of this and other policies is essential to contain the economic fallout.

Given the uncertainty surrounding the extension of the pandemic and of the measures necessary to mitigate it, we have chosen to present our forecasts on ranges for 2020 and 2021. These ranges differ on the hypotheses used over the extension of the restrictive measures, and on the strength of the recovery after they are lifted. We have further downgraded our forecast for GDP growth to the range of -2.6% to -4.7% in 2020. But we continue to call for one more rate cut in the Selic rate this quarter, to 3.25%, where we believe it will remain until the end of the year, in order to ease financial conditions for the recovery.

| PROJEÇÕES ECONÔMICAS                 | 2015   | 2016   | 2017  | 2018  | 2019  | 2020P                 | 2021P                 |
|--------------------------------------|--------|--------|-------|-------|-------|-----------------------|-----------------------|
| Crescimento do PIB (%)               | -3,5%  | -3,3%  | 1,3%  | 1,3%  | 1,1%  | <b>-2.6% to -4.7%</b> | <b>4% to 5.2%</b>     |
| Inflação (%)                         | 10,7%  | 6,3%   | 2,9%  | 3,7%  | 4,3%  | <b>1.8% to 2.2%</b>   | <b>3.1% to 3.3%</b>   |
| Taxa de Desemprego (%)               | 9,6%   | 12,6%  | 12,4% | 12,2% | 11,7% | <b>12% to 13.5%</b>   | <b>11.5% to 12.5%</b> |
| Taxa Selic (%)                       | 14,25% | 13,75% | 7,00% | 6,50% | 4,50% | <b>3,25%</b>          | <b>5,0%</b>           |
| <b>Contas Externas</b>               |        |        |       |       |       |                       |                       |
| Balança Comercial (US\$ bi)          | 20     | 48     | 67    | 53    | 39    | <b>33 to 40</b>       | <b>40 to 46</b>       |
| Saldo em Conta Corrente (US\$ bi)    | -59    | -23    | -10   | -42   | -51   | <b>-40 to -45</b>     | <b>-45 to -50</b>     |
| Saldo em Conta Corrente (% do PIB)   | -3,3%  | -1,3%  | -0,7% | -2,2% | -2,8% | <b>-2,2% to -2,7%</b> | <b>-2,2 to -2,5%</b>  |
| <b>Política Fiscal</b>               |        |        |       |       |       |                       |                       |
| Resultado Primário Fiscal (% do PIB) | -1,9%  | -2,5%  | -1,8% | -1,6% | -0,9% | <b>-6.5% to -7.5%</b> | <b>-1.5% to -2.5%</b> |
| Dívida Bruta do Governo (% do PIB)   | 66,2%  | 69,4%  | 73,7% | 77,2% | 75,9% | <b>83% to 86%</b>     | <b>82% to 85%</b>     |