BANK OF COMMUNICATIONS BBM

# Macro Monthly Letter

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# Scenarios for 2024 and 2025

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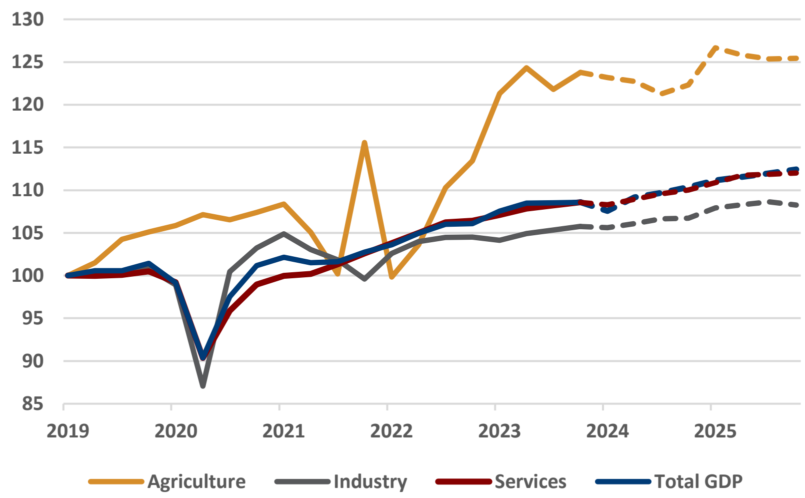
The Brazilian economy performed remarkably well in 2023: inflation fell from 5.8% to 4.4%, and despite the monetary tightening that began in 2021 and persisted until the middle of this year, activity remained resilient, with growth of about 3% and unemployment lower than at any time since 2015. Strong growth in agricultural production and spillover effects on other sectors supported overall economic activity. For 2024, the monetary loosening cycle under way in Brazil and favorable external conditions point to continuing, albeit decelerating, economic growth (Figure 1).

**Figure 1: GDP growth forecast (Level SA, 2019=100)**




Source: BOCOM BBM, BCB

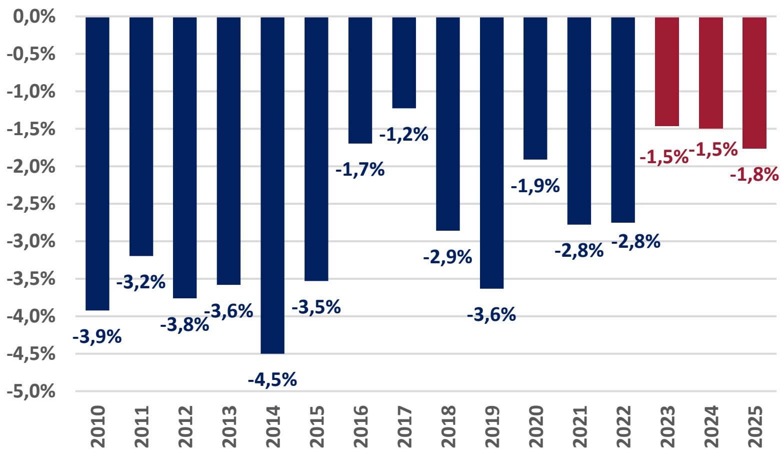
The lagging effects of monetary policy explain part of this deceleration. We project 1.3% growth led by the service sector next year. Conditions are favorable for growth in the industrial sector, but only thanks to specific segments such as mining and oil production, while construction, manufacturing and other segments that follow the business cycle will face stronger challenges. The agricultural sector will hold steady, which is by no means imply bad news considering its outstanding growth of about 16% in 2023. The grain crop is set to fall slightly, according to estimates, but adverse climate conditions due to the particular intensity of this El Niño could contribute to a steeper fall.

The more adverse weather may also affect next year's inflation, especially food inflation, which is already showing signs of accelerating in recent IPCA readings. In addition, normalization of the prices of industrial goods due to the end of supply chain bottlenecks eliminates a major driver of disinflation seen in 2023. Pass-through of the tax hikes called for by the government's fiscal agenda will also make a significant contribution to next year's inflation. As a result, while inflation benefited in 2023 from the massive shock to tradables, such as agricultural commodities and other goods used in commerce, which had secondary effects on core inflation rates and services inflation, 2024 is unlikely to see disinflation continuing at a similar pace because of larger challenges such as only partial re-anchoring of inflation expectations. We project 4% by the end of next year.

In 2025, we expect inflation to remain above target in light of significant medium-term risks, including moves to make the fiscal framework flexible, changes to the composition of the Central Bank of Brazil's Monetary Policy Committee (Copom), and a new rule allowing annual adjustments to the minimum wage (used to calculate pensions, welfare and unemployment insurance) to exceed inflation by the amount corresponding to GDP growth two years previously.

In the balance of payments, abundant exports of agricultural and mineral commodities combined with a fall in prices of imported goods led to a record trade surplus in 2023. This result was sufficient to keep the current-account deficit at historically low levels despite significant deficits in the services account and primary incomes. Although the inflow of foreign direct investment is in decline, reflecting the gradual deceleration of economic growth and lower corporate profitability in Brazil and abroad, it has been more than sufficient to assure healthy financing of the current-account deficit. We continue to expect a sound balance of payments in 2024 and 2025 (Figure 2).

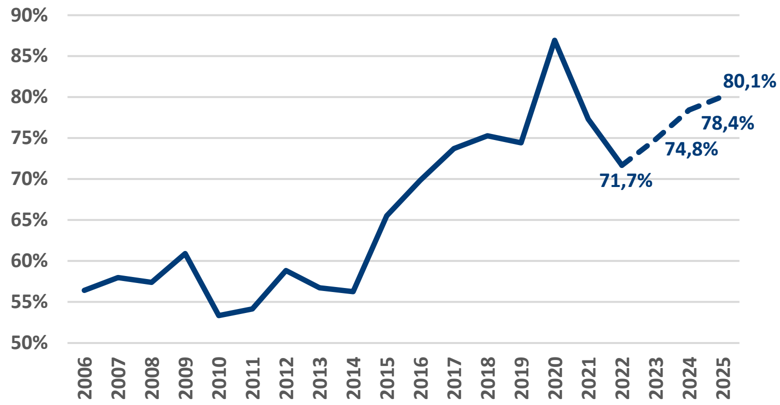
**Figure 2: Current Account (% GDP)**




Source: BOCOM BBM, BCB, IBGE

With regard to the fiscal outlook, the fiscal framework passed by Congress in 2023 establishes a new concept of balanced national accounts, permitting a minimum of real growth in expenditure as long as tax revenue rises enough to assure the targeted primary result. However, difficulties in passing the necessary measures to raise tax revenue and the potential for partial spending freezes (contingenciamentos) represent risks to the credibility of the new rules in their first year in force. Although the government has reiterated its commitment to a zero primary deficit, we project a 1% deficit in 2024, corresponding to a rise in the debt-to-GDP ratio to 78.4%. Decelerating economic growth, attempts to authorize additional spending as an "exception" to the rules and rising outlays for court-ordered payment of federal debts (precatórios) also represent risks to the trajectory of the public debt (Figure 3).

**Figure 3: Debt-to-GDP ratio**




Fonte: BOCOM BBM, BCB, IBGE

Structurally speaking, the tax reform bill now before Congress adds to several other reforms passed in recent years (such as the TLP, the basic sanitation framework and the new labor laws) and will significantly simplify the Brazilian tax system while also enhancing business efficiency and competitiveness. This reform improves the economy's long-term growth prospects, but the slow pace of the transition from the old regime to the new one and the need for additional implementing legislation makes estimates of gains uncertain.

Conjunctural and structural conditions will put Brazil in an economically favorable situation in 2024 and 2025. Our macroeconomic projections are shown in the table below.

| ECONOMIC FORECASTS | 2020 | 2021 | 2022 | 2023F | 2024F | 2025F |
|---|---|---|---|---|---|---|
| GDP Growth (%) | -3.3% | 4.8% | 3.0% | 2.9% | 1.3% | 2.0% |
| Inflation (%) | 4.5% | 10.1% | 5.8% | 4.4% | 4.0% | 4.0% |
| Unemployment Rate (eoy ,%) | 14.2% | 11.1% | 7.9% | 7.8% | 8.4% | 8.5% |
| Policy Rate (eoy, %) | 2.0% | 9.3% | 13.75% | 11.75% | 9.50% | 8.75% |
| External Accounts | | | | | | |
| Trade Balance MDIC (US$ bn) | 50 | 61 | 62 | 95 | 87 | 78 |
| Trade Balance (US$ bn) | 32 | 36 | 44 | 77 | 67 | 58 |
| Current Account Balance (US$ bn) | -28 | -46 | -54 | -32 | -34 | -43 |
| Current Account Balance (% of GDP) | -1.9% | -2.8% | -2.8% | -1.5% | -1.5% | -1.8% |
| Fiscal Policy | | | | | | |
| Central Government Primary Balance (% of GDP) | -9.8% | -0.4% | 0.5% | -1.2% | -1.0% | -0.9% |
| Government Gross Debt (% of GDP) | 86.9% | 77.3% | 71.7% | 74.8% | 78.4% | 80.1% |