



GDP is expected
to contract by
8.0% in the
second quarter
and by -4.8% in
2020

August 2020

- We revised our GDP forecast from -6.0% to -4.8% in 2020 and from + 2.5% to + 3.0% in 2021.

Reasons:

- Economic activity contracted less in the second quarter than initially expected.
- Fiscal and monetary stimuli for households and businesses mitigated the recession.
- Pandemic effects act heterogeneously across sectors and still impose high uncertainty on labor market trajectory and aggregate demand in the medium term.

	Agriculture	Industry	Services sector	GDP
2020	2.6	-5.0	-5.2	-4.8
2021	2.8	5.9	2.2	3.0

Source: XP Investimentos

Brazil may follow the global economic cycle of recovery but considering its own characteristics and its own time in the pandemic chronology. Aspects that characterize Brazil's reality cannot be ignored, such as the fact that Brazilian idleness is greater than that one observed in advanced economies and it already was even before the pandemic (which could partly explain a less intense fall in Brazilian GDP in the second quarter of this year, comparing it with US economy). In addition, the approval of structural reforms is essential for the strongest recovery in 2021.

Another essential aspect of the pace of Brazilian economic recovery is the country's aggregate demand. Social distance measures have significantly affected the service sector, making it hard to project the dynamics of supply/demand per labor. Even with the 2017 labor reform, the Brazilian labor market is still considered rigid. However, the government's programs for sustaining and preserving formal jobs have proven successful. On the side of the informal workforce, the emergency aid program that reached, according to DataPrev, indirectly up to 124 million people, also contributes to an increase in the mass of income of a population with a greater propensity to consume.

Nevertheless, Brazil Central Bank also has a fundamental role in this recovery. Among the scenario in which the health risks dissipate and the agents' confidence gradually returns, the monetary policy with Selic at 2.00% per year (and in a stimulating scenario) will be able to contribute positively to economic activity.

Furthermore, in our assessment, it seems unlikely that there will be a lockdown or more restrictive social distancing measures again in the coming months, even with Brazil still forming a high plateau in the number of cases and deaths. Positive news about advances in vaccine stages is already reflected in financial market around the world and reinforces the perception of activity recovery over the next quarters.

	2Q20		2020
	YoY, %	QoQ, %	
Agriculture	2.3	1.1	2.6
Industry	-12.6	-12.2	-5.0
Extractive	3.1	-3.7	-0.7
Transformation	-18.3	-15.9	-6.6
Construction	-11.4	-4.7	-5.1
SIUP	-7.1	-6.6	-3.8
Services sector	-9.6	-8.1	-5.2
Retail sales	-12.7	-10.6	-6.7
Transport	-16.4	-13.0	-7.2
SIC	-4.3	-1.7	-2.0
Intermediation	2.0	0.3	1.5
Other services	-22.7	-18.9	-13.2
Real Estate	-3.0	-3.1	-0.9
Government	-2.0	-1.6	-1.1
Taxes	-11.3	-	-5.4
GDP	-9.8	-8.0	-4.8
Household Consumption	-9.5	-7.5	-5.3
Government Consumption	-0.4	-0.6	0.0
GFCF	-22.0	-20.2	-11.3
Export	-10.7	-6.8	-4.9
Import	-14.0	-11.3	-6.3

Source: XP Investimentos

Agriculture is practically unscathed by the new coronavirus pandemic and is expected to grow + 2.6% in 2020. Industry, with greater recovery dynamics, is expected to retract -5.5% in 2020 and accelerate + 5.9% in 2021. The service sector, which is the most affected by social distancing measures, is expected to recover gradually after a projected drop of 5.2% in 2020 and an increase of 2.2% in 2021.

The second quarter of 2020

The first major revision factor was the performance of economic activity in the second quarter of this year. After dropping 1.5% (it would be revised to -2.5%) in the first quarter of 2020, expectations for the second quarter reached -13.0% YoY. However, after total economic paralysis in April, the less adverse performance for the manufacturing and retail industry in May and June managed to sustain the “less negative” decline in the quarter. With observed PIM-PF (industry) and PNAD-Continuous (labor market) indicators and June PMC (retail sales) and PMS (services sector) forecasts, we project that the Brazilian economy may have a record contracting of -8.0% in the second quarter of this year after contracting by 2.5% (revised) in the first quarter.

Homebuilders were not relatively paralyzed during the pandemic under the seal of being considered an essential activity. However, from the perspective of the National Accounts methodology, there is doubt about the behavior of the sector's labor force, since from the input side (SNIC and ITCC) the data point to a good recovery. Credit data also indicate that, unlike other crises, real estate financing did not lose traction until June. Trade, underpinned by income transfer programs, had a less negative trajectory than initially projected. These segments are relevant because of their multiplier effect on the Brazilian economy.

On the other hand, the service sector (excluding commerce and public administration) suffers the greatest losses and its recovery depends intrinsically on the health issue in the first moment and on the gain of confidence in consuming by the population in a second moment. Highly labor-intensive, this sector is the biggest source of uncertainty about projections of economic activity in the short and medium terms.

GDP forecast

The degree of volatility in GDP expectations for 2020 is still quite high and atypical for this period of the year. The large gap in the data's release on official activities (compared to advanced economies) imposed an increase in high frequency indicators relevance, such as energy consumption data and weekly ICVA. In any case, industry and retail data have been showing results better than market consensus and this decreases more negative expectations for the rest of the year. However, as mentioned, the degree of impact on each segment of the economy was quite heterogeneous and the second quarter GDP disclosure on September 1 will be fundamental for a greater sectorial understanding of how the pandemic has been impacting the Brazilian economy. Anyway, expectations for this year's GDP drop are "less negative" than they were a few months ago, and the recovery is a little stronger.

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