

Blue Notes | Weekly | October 11, 2019

Gradual recovery and low inflation in Brazil and US-China 'mini-deal' expectations. This week's IBGE indicators portrayed well our views around the economic scenario. The September IPCA, as well as, the August retail and services surveys showed that the economic recovery is being led by the private consumption, but it is taking place gradually and, given the elevated idle capacity, is not generating inflation pressures. On the external front, the ups-and-downs around speculations about US-China trade negotiations drove the markets and ended the week on a more positive tone on the back of expectations of a 'mini-deal' that would avoid a planned hike in tariffs next week.

Low inflation hints weak activity, but it can push consumption up ahead. Recent inflation numbers have been on the low side and they certainly reflect the high output gap in the economy. In the short run tough, low inflation can push consumption up by improvements in the disposable income of households. An important part of the recent inflation deceleration has been on the back of lower increases in food prices which should open room for consumers to spend in other items. Consumption will also gain the support from the FGTS (Length-of-Service Guarantee Fund) release that has happened since September and by consumption confidence that has been gradually on the rise.

We keep our call for 0.7% and 2.2% GDP growth for this year and next. Next Monday, the Central Bank will release the monthly GDP estimate (IBC-Br) that should print on the negative side, given the tamed performance in the services and retail sectors (-0.2%*m/m* sa and 0.1%*m/m* sa) and despite the positive industrial performance in the month. We keep our call for a small deceleration in the 3Q19 GDP with a reacceleration in the 4Q19, closing this year at 0.7% and improving to 2.2% in 2020.

'Mini-deal' expectation brings relief to the markets. Markets were focused this week in the American and Chinese talks on the trade war. Volatility has been high this week in terms of expectations regarding the deal and as of Friday, media outlets were suggesting a 'mini-deal' could be reached. This deal would comprehend a postponement of tariff increases that were set to be increased by the end of this month. Despite this expectation, a final solution to the trade war issue doesn't seem likely and despite the short-term relief, the subject should be back to the spotlight sooner rather than later.

Eyes in economic activity releases in Brazil and China. With geopolitical risks less pronounced in the short term, the next week focus should be on growth data, with IBC-Br being in Brazil and 3Q19 GDP growth in China.

