

While current inflation remains positive, risk balance worsened

Overview

- **Despite the contained current inflation, worsened financial conditions led us to revise our IPCA estimate to 4.4% in 2018.** The IPCA fell 0.09% in August, in line with our forecast, driven mainly by lower food prices. Core inflation, in turn, picked up momentum, but remains at a comfortable level. This upswing was already expected and will likely persist in the coming months, driven mainly by prices of manufactured goods. Prospectively, even if the inflation scenario remains positive, risk balance has taken a turn for the worse. The still challenging global scenario for emerging economies and lingering economic uncertainties drove the Brazilian currency exchange rate to nearly BRL 4.15/USD. Considering that this adverse global scenario will likely persist, we revised our exchange rate forecast to BRL/USD 3.90 for YE2018. We also raised our IPCA forecast to 4.4%, mostly to higher regulated prices (especially fuel prices). We believe that the exchange rate pass-through to market prices will be below the historical average, due to subdued growth.
- **The transition from the second to the third quarter remains moderate.** Manufacturing output dropped 0.2% in July, surpassing the 1.6% and 1.5% drops expected by us and the market, respectively. The month's biggest surprise was the rise in intermediate goods. On the other hand, production of consumer goods (durable and non-durable) and capital goods remained weak. In fact, BRL depreciation in recent months and the waning confidence of business owners and consumers will likely continue to weigh on consumption and investment. This context reinforces our scenario regarding a GDP increase of 0.2% in the third quarter and 1.1% in 2018 as a whole.
- **August industrial indicators confirm showed more evidence of the gap between growth in the U.S. and the rest of the world.** The August Purchasing Managers' Index (PMI) pointed to steady global growth, but with a widening gap between regions. While industrial activity in the Eurozone and UK lost some steam throughout the third quarter, indicators show that activity in the U.S. is accelerating. Strong U.S. growth, bolstered by a dynamic job market and the gradual acceleration of inflation, is consistent with our forecast of two additional interest rate increases in 2018 and two more in 2019 (bringing the benchmark interest rate to 3.0%). When added to the multiple outbreaks of volatility worldwide (e.g. trade war, tension between the U.S. and Turkey, Argentina, etc.), we believe that the environment will remain very challenging for emerging markets, ultimately increasing the volatility in this asset class.

Weekly outlook

- **Domestic highlights include the release of trade and service data for July.** We estimate that retail sales remained more or less stable in July, while the services sector may have decelerated slightly. Together with industrial production data, these indicators will likely reinforce expectations of gradual recovery in the quarter. The IGP-10 for September will also be released this week (we forecast 0.92%), still suggesting substantial pressure on wholesale prices.
- **Highlights in the external agenda include the meetings of the European Central Bank (ECB), the Bank of England (BoE) and the Central Bank of Turkey.** In light of the recent underwhelming performance of the economy and inflation cores in the Eurozone, we believe the ECB's announcement will be on a lighter tone. Similarly, the BoE will likely tone down its language after the surprise in the last meeting. In Turkey, the Central Bank may raise its policy rate by 300bps in order to contain the recent slump of the Turkish lira. U.S. inflation indicators will also be released (we expect more evidence of a gradual rise in inflation). At the same time, Chinese data for August may indicate more moderate economic activity in the third quarter.

Time	Country	Event	Forecast (Bloomberg)	Forecast (Depec)
Monday 09/10				
08:00	Brazil	FGV: Consumer Price Index (IPC-S) (weekly)		
08:25	Brazil	BCB: Focus Survey		
15:00	Brazil	MDIC: Trade Balance (weekly)		
-	Brazil	Serasa experian: Retail Activity Index (Aug)		
20:50	Japan	GDP (2Q - F)	0.7% (QoQ)	
22:30	China	CPI (Aug)	2.1% (YoY)	
Tuesday 09/11				
08:00	Brazil	FGV: IGP-M (1st preview) (Sep)		
09:00	Brazil	IBGE: Agricultural production Survey (Aug)		
09:00	Brazil	Conab: 12th Grains crop survey 2017/2018		
09:00	Brazil	IBGE: Industrial Production - regional (Jul)		
06:00	Germany	ZEW Survey Expectations (Sep)		
Wednesday 09/12				
05:00	Brazil	FIPE: Consumer Price Index (weekly)		0.35%
12:30	Brazil	BCB: Currency Flows (weekly)		
06:00	Eurozone	Industrial Production (Jul)		
Thursday 09/13				
09:00	Brazil	IBGE: Retail sales (PMC) (Jul)		0.1% (MoM)
03:00	Germany	CPI (Aug - F)		
08:00	United Kingdom	Central bank meeting		0.75%
08:45	Eurozone	Central bank meeting		0.00%
09:30	USA	Initial Jobless Claims - Weekly		
09:30	USA	CPI (Aug)	0.3% (MoM)	
20:00	Peru	Central bank meeting		2.75%
23:00	China	Industrial Production (Aug)	6.6% (YoY)	
23:00	China	Fixed Assets Investments (Aug)	5.7% (YoY)	
Friday 09/14				
08:00	Brazil	FGV: IGP-10 (Sep)		0.85% (MoM)
09:00	Brazil	IBGE: Services Sector Volume (PMS) (Jul)		-0.3% (MoM)
10:15	USA	Industrial Production (Aug)	0.3 (MoM)	
11:00	USA	University of Michigan Sentiment (Sep - P)	96.0	

	2016	2017	2018	2019
Consumer inflation - IPCA (%)	6.29	2.95	4.40	4.25
GDP growth (%)	-3.6	1.0	1.1	2.5
Industrial Production (%)	-6.4	2.5	1.5	2.7
Retail Sales (%)	-8.7	4.0	5.0	4.5
Unemployment Rate (% of labor force, avg)	11.5	12.7	12.5	12.3
Outstanding Credit Growth (%)	-3.5	-0.5	4.0	8.3
Trade Balance (USD bn)	45.0	64.0	60.4	61.1
Current Account (USD bn)	-23.5	-9.8	-9.9	-8.5
Exchange Rate (BRL/USD, eop)	3.26	3.31	3.90	3.80
Selic Rate (% eop)	13.75	7.00	6.50	8.00
Primary Balance (BRL bn)	-155.8	-111	-132.7	-94.9
Gross Debt (% of GDP)	70.0	74.0	75.7	76.5

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