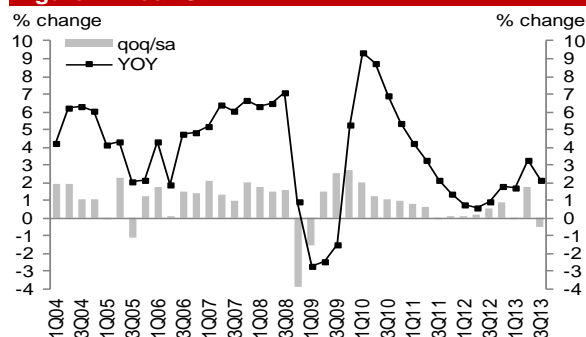


3Q13 GDP result: Recovery disappoints with 0.5% contraction qoq/sa

Interrupting the recent and gradual recovery of growth seen in 1H13, Brazil's 3Q13 GDP result disappointed with a decline in economic activity and the enduring imbalance of growth drivers. Resilient private consumption led growth again, while fixed investment contracted and exports slowed.

Real GDP contracted 0.5% quarter-on-quarter (qoq/sa) in 3Q after having increased 1.8% qoq/sa in 2Q, according to results released on Tuesday. In year-on-year terms, GDP rose 2.2% in 3Q versus 3.3% in 2Q. (Figure 1.) Key data revisions include a downward adjustment for 1Q to 0.0% qoq/sa (from 0.63% previously) and an upward adjustment for 2Q to 1.8% qoq/sa (from 1.5%). For 2012, growth was revised upwards to 1.0% (from 0.9%).

Figure 1: Real GDP



Source: IBGE; BTMU Economic Research (NY).

Figure 2: Real GDP

% variation	quarter-on-quarter/sa					year-on-year				
	3Q12	4Q12	1Q13	2Q13	3Q13	3Q12	4Q12	1Q13	2Q13	3Q13
Total	0.6	0.9	0.0	1.8	-0.5	0.9	1.8	1.8	3.3	2.2
Supply-side										
Agriculture	7.7	-6.7	5.8	4.2	-3.5	4.0	-7.0	13.2	11.6	-1.0
Industry	0.8	0.0	-0.4	2.2	0.1	-0.7	0.0	-1.2	2.7	1.9
Services	0.5	0.9	0.1	0.8	0.1	1.4	2.8	1.7	2.4	2.2
Demand-side										
Private consumption	1.0	1.1	-0.1	0.3	1.0	3.6	4.2	2.3	2.6	2.3
Public consumption	-0.4	1.0	-0.5	0.5	1.2	3.4	4.4	2.4	0.8	2.3
Fixed investment	-1.1	1.8	4.2	3.6	-2.2	-5.6	-4.2	3.2	9.1	7.3
Exports	1.2	3.7	-5.1	6.8	-1.4	-3.2	2.1	-5.7	6.3	3.1
Imports	-6.1	8.2	5.4	0.3	-0.1	-6.4	0.5	7.5	7.7	13.7

Source: IBGE; BTMU Economic Research (NY).

More of the same: Growth composition upsets prospects of re-balanced, broad-based recovery

On the demand side, consumption continues to be the main growth driver of the economy. (Figure 2.) Private consumption, which accounts for two-thirds of GDP, picked up momentum on account of a tight labor market, real wage gains, and slowly declining inflation to register growth of 1.0% qoq/sa compared to 0.3% in 2Q. While remaining the driving force for growth, it has nevertheless moderated upon a slowed credit market, still-high inflation, and less optimism. Indeed, private consumption grew 2.3% yoy and 2.8% in the four quarters through 3Q, decelerating from growth of 3.2% in 2012 and 4.1% in 2011.

In 3Q, public consumption rose 1.2% qoq/sa (vs 0.3% in 2Q) and 2.3% yoy (vs 0.8% in 2Q) despite the deterioration of fiscal balances and inflation pressures.

Fixed investment was the major disappointment. After having expanded for three consecutive quarters in sequential terms, it contracted 2.2% qoq/sa in 3Q. (Figure 3.) Its increase of 7.3% yoy, however, is attributed to a weak result in 3Q12. Domestic and external factors combined to restrict investment conditions. In the context of a deteriorated domestic investment climate and the monetary tightening cycle, the combination of global financial market volatility and a weakened BRL lowered confidence levels, widened Brazil's 5-yr CDS spread, and raised the costs of capital and imports to slow investment growth. (Figure 4.)

Net exports dragged on growth. Exports fell 1.4% qoq/sa upon lower prices and volumes as external demand is weak. Imports dropped 0.1% qoq/sa.

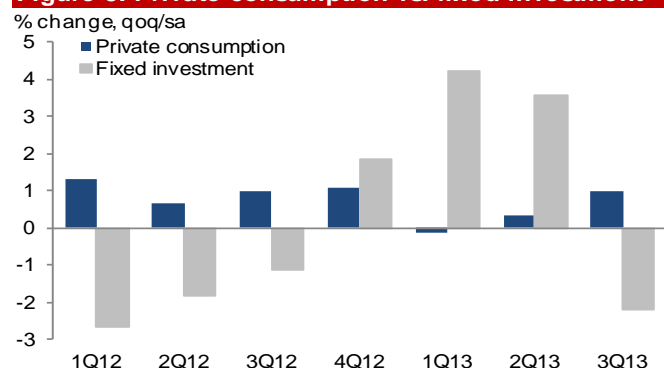
On the supply side, services recorded a notable deceleration as it grew 0.1% qoq/sa (vs 0.8% in 2Q). Industry also struggled; it rose 0.1% qoq/sa (vs 2.2%).

With low growth-high inflation dynamic, monetary tightening cycle is closer to the end

Activity indicators for 4Q show some improvement, led by retail sales, which should place growth at 2.3% in 2013. As the recovery has not seen sustained improvement in key sectors or the investment climate, growth will stay modest near 2.1% yoy in 2014. With moderated—but high—inflation, consumption will remain the main growth driver, while the concessions and World Cup preparations should support a slight cyclical acceleration of investment from 3Q. Yet, risks are to the downside due to the prospects of lower commodity prices, tighter financial conditions, and a higher risk premium. Investment is fragile in a low growth-high inflation environment where uncertainty surrounds government policy. Brazil's investment ratio is 19% of GDP, below the regional average of 22%.

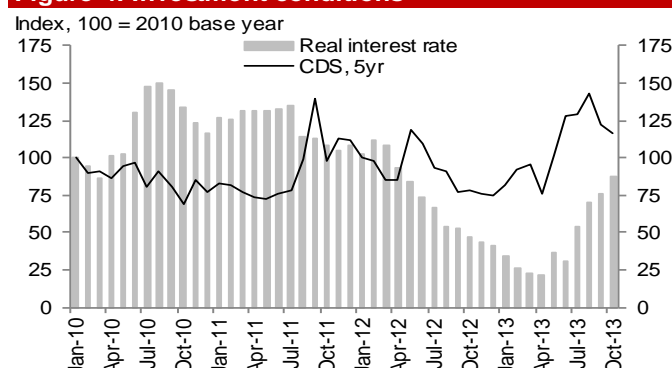
Mediocre growth is likely to prompt the BCB to conclude the monetary tightening cycle in early 2014. The chance for holding has risen. However, we expect a 25bp hike in January, raising the SELIC to 10.25%, where it will remain for the rest of 2014 amid the run-up to the October election and concerns over growth.

Figure 3: Private consumption vs. fixed investment



Source: IBGE; BTMU Economic Research (NY).

Figure 4: Investment conditions



Source: Central Bank; Bloomberg; BTMU Economic Research (NY).



For historical data and commentary following BTMU's Economic News Releases, see our website at: <http://www.bk.mufg.jp/report/ecolatin2013/index.htm>

The information herein is provided for information purposes only, and is not to be used or considered as an offer or the solicitation of an offer to sell or to buy or subscribe for securities or other financial instruments. Neither this nor any other communication prepared by The Bank of Tokyo-Mitsubishi UFJ, Ltd. (collectively with its various offices and affiliates, "BTMU") is or should be construed as investment advice, a recommendation to enter into a particular transaction or pursue a particular strategy, or any statement as to the likelihood that a particular transaction or strategy will be effective in light of your business objectives or operations. Before entering into any particular transaction, you are advised to obtain such independent financial, legal, accounting and other advice as may be appropriate under the circumstances. In any event, any decision to enter into a transaction will be yours alone, not based on information prepared or provided by BTMU. BTMU hereby disclaims any responsibility to you concerning the characterization or identification of terms, conditions, and legal or accounting or other issues or risks that may arise in connection with any particular transaction or business strategy. While BTMU believes that any relevant factual statements herein and any assumptions on which information herein are based, are in each case accurate, BTMU makes no representation or warranty regarding such accuracy and shall not be responsible for any inaccuracy in such statements or assumptions. Note that BTMU may have issued, and may in the future issue, other reports that are inconsistent with or that reach conclusions different from the information set forth herein. Such other reports, if any, reflect the different assumptions, views and/or analytical methods of the analysts who prepared them, and BTMU is under no obligation to ensure that such other reports are brought to your attention.