



GDP Observatory

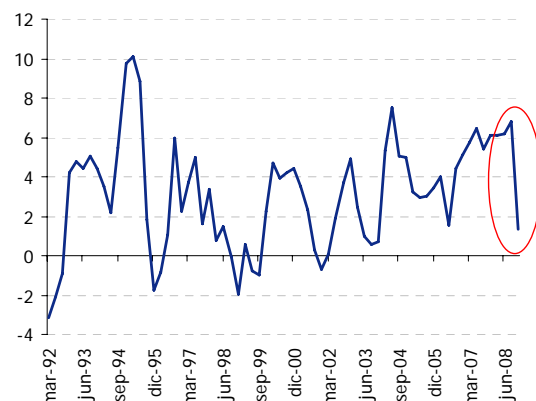
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Brazilian GDP surprises negatively in Q4 2008, plunges 3.6% q-o-q and puts economy on track for a recession. Yearly growth was 5.1%.

- The 3.6% fall was higher than expected by BBVA (3.0%) and much higher than forecasted by the market (2.3%). The fall is also the highest of the series (which starts in 1996).
- **With the exception of public consumption, all other demand components displayed very sharp variations in Q4 2008.** Investments and private consumption declined more than expected, by 9.8% and 2% q-o-q respectively. Public consumption expanded 0.8%. Exports contracted 2.9% and imports dropped 8.2% as both international trade and capital flows collapsed after the beginning of the crisis. The contribution of the external demand to the GDP growth during the fourth quarter was -0.6% in comparison to -1.1% in the third quarter of the year.
- Considering supply-side components, the GDP of the industrial activities showed the highest drop (7.4% q-o-q) as had been suggested by Industrial Production data released beforehand. The agriculture sector displayed a 0.5% contraction and the services dropped 0.4% in comparison to Q3 2008. **Weak demand for industrial products – and not falling commodities prices - was the main driver of the contraction.**
- In comparison to the last quarter of 2007, the economy expanded 1.3% in Q4 2008. In the previous quarter the GDP had gained 6.8% y-o-y. The growth decline between Q3 2008 and Q4 2008 was very intense (the highest decline since 1995).
- **2008 GDP growth was 5.1%, slightly less than the 5.2% forecasted by BBVA.**
- **Our current forecasts for 2009 and 2010 are 0.9% and 1.5% respectively. These numbers are now definitively downwards tilted.**
- Some activity indicators available for the Q1 2009 shows that the economy continued to contract and therefore **the country is expected to enter technically in recession in the first quarter of the year.** Nonetheless, the contraction pace should slow down in comparison to the 3.6% q-o-q observed in Q4 2008. **We expect GDP to contract around 2% q-o-q in Q1 2009.**
- **GDP results strength the view that the Central Bank will cut interest rates aggressively during its next meetings. For this week's meeting the 100 bps cut previously expected is now taken**

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Brazilian GDP
(y-o-y %)



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(y-o-y %)

	Q4 07	Q3 08	Q4 08	2008	2009 (f)
GDP	6.1	6.8	1.3	5.1	0.9
Private Consumption	7.2	7.3	2.2	5.4	1.5
Public Consumption	3.6	6.4	5.5	5.6	2.0
Investments	16.0	19.7	3.8	13.8	-3.0
Exports	6.2	2.0	-7.0	-0.6	-2.0
Imports	23.5	22.8	7.6	18.5	-4.0

as given and a higher cut shouldn't come as a surprise. The 10.25% rate forecasted for the end of the year is now downward biased.

- Interest rates declined in future markets right after the announcement of GDP figures. On the other hand, the Brazilian Real appreciated and the IBOVESPA rose following external markets and paying less attention to GDP numbers. Public authorities admitted that fiscal targets for 2009 could be reduced, opening more space for countercyclical fiscal policies.