Economic Watch

Brazil

Madrid, 25 May 2011
Economic Analysis

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Brazil: positive terms of trade have avoided further deterioration of the current account

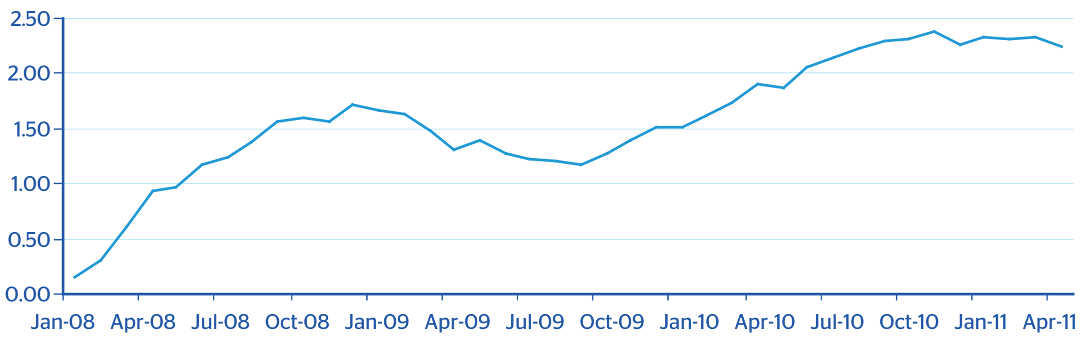
- The yearly current account deficit was equal to 2.25% of GDP in April. The deficit has been around 2.3% since September 2010. A further deterioration of the current account has been avoided by very positive terms of trade. Capital inflows - especially FDI which reached 2.93% of GDP in April - continue providing very ample funding for the current account deficit.

- The current account deficit reached USD 3.488 million in April and has now accumulated USD 48.918 million (2.25% of GDP) in the last 12 months.

- This month's deficit was lower than we expected (USD 4.500 million) and even lower than the market consensus (USD 4.859 million). The current account deficit was below both the figure observed in March (USD 5.676 million) and the deficit recorded in April 2010 (USD 4.615 million).

- As a share of GDP, the current account deficit has remained broadly stable since September of 2010 when it reached 2.29% (see graph below).

Chart 1
Current account deficit (% GDP; accumulated in the last 12 months)



Source:Central Bank of Brazil

- A further deterioration in external accounts has been avoided in the last few months by the good performance of exports, which in turn have been supported by exceptionally positive terms of trade.

- More precisely, exports of goods increased 33%y/y in April and 31%y/y in the first four months of the year. This compares relatively well with the performance of imports, which grew 32%y/y in April and 27%y/y in the January-April period.

- The recent evolution of the terms of trade help to understand the positive evolution of exports vis-a-vis imports: the prices of exports were 26%y%y higher in Q1 11 than in Q1 10, while on the other hand, the prices of imports were "just" 12%y/y higher. As a consequence, Brazilian terms of trade improved 13%y/y in the period.
- In this environment, the trade balance reached USD 1.863 million in April (USD 5.036 million in the Jan-April period), which is 45%y/y higher than in the same month last year (133%y/y higher than in Jan-April of 2010).
- The lower than expected current account deficit observed in April was not only a result of a higher trade balance but also of some moderation of the deficit in the service and income balance, which was equal to USD 5.566 million in April (in comparison to the average of the previous three months: USD 6.223 million). This moderation is probably related to the slowdown of domestic demand in the beginning of the second quarter of the year.
- We expect terms of trade to ease in coming quarters and the current account deficit to reach USD 65 billion (2.6% of GDP) by the end of 2011, but if terms of trade refrain from dropping as expected, the current account deficit could end up being lower than we are currently forecasting.
- Regarding the funding of the current account deficit, data released today show that foreign capital continues to flood into the country: in April, the capital and financial account surplus reached USD 10.813 million and accumulated USD 125.604 million (5.8% of GDP) in the last 12 months.
- FDI inflows continued to be robust and surprised markets to the upside: they reached USD 5.512 million in April and accumulated USD 63.682 million (2.93% of GDP) in the last 12 months, which represents 51% of net capital inflows recorded in the balance of payments..

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