

Brazil Overview

Macro and Political Landscape

September 2018



Tightening EM financial conditions and political uncertainties slowing Brazil's economic recovery.

Key observations from our research:

- Brazilian GDP rose 1.0% on the second quarter of the year when compared to the second quarter of 2017, consolidating the fifth straight quarter with economic growth after a 12-quarter recession period.
- Recent improvements on some activity indicators, such as private indebtedness and net job creation, are positively impacting consumer and industry confidence levels.
- Despite that, the rate of recovery is increasingly diminishing ahead of the presidential elections in October, with important challenges regarding the equalization of Brazil's fiscal situation, a wide-open presidency race and worsening emerging market conditions, which is leading to a large BRL depreciation and financial outflow.
- Inflation and base interest rates are in historically-low levels, but may face upwards pressure from political and macroeconomic events in the next months.
- Brazilian financial markets started strong in 2018, with 3 IPOs amounting to USD1.8billion (97% increase in volume when compared to 1Q2017), but activity has since slowed down as companies await for some definition on the political front and a more stabilized currency.
- Regarding the presidential elections, right-wing congressman Jair Bolsonaro still leads polls with 28% of vote intentions (as of September 18th), trailed by the Worker's Party candidate Fernando Haddad.



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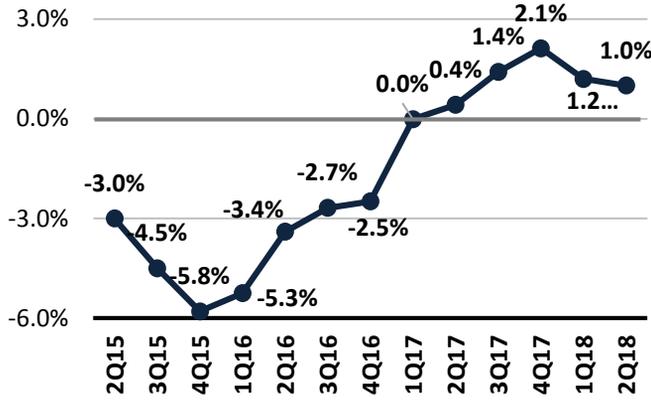
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Key Macroeconomic Indexes

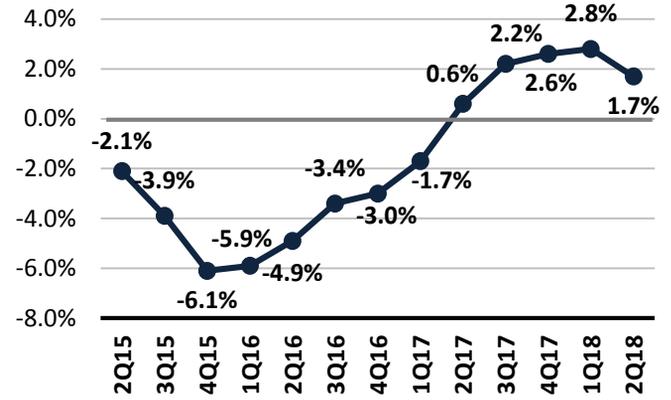
GDP Growth – Quarterly

% Quarter over Quarter



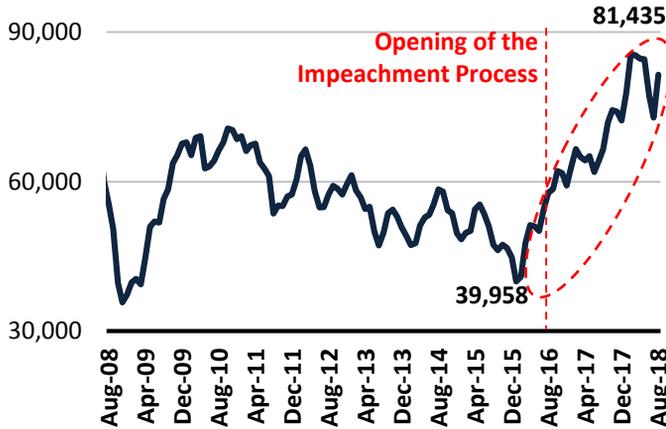
Consumption Growth – Quarterly

% Quarter over Quarter



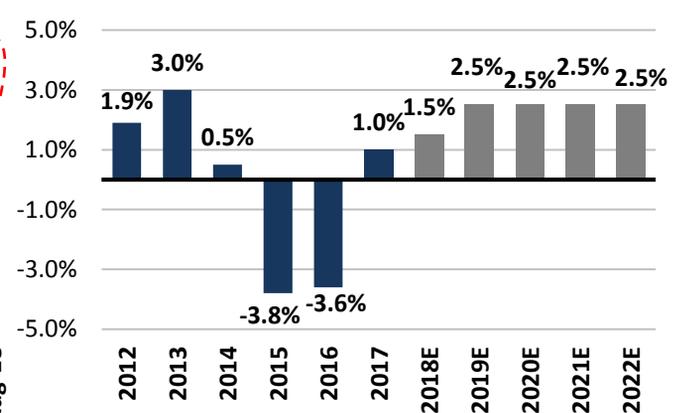
Bovespa Index

Points



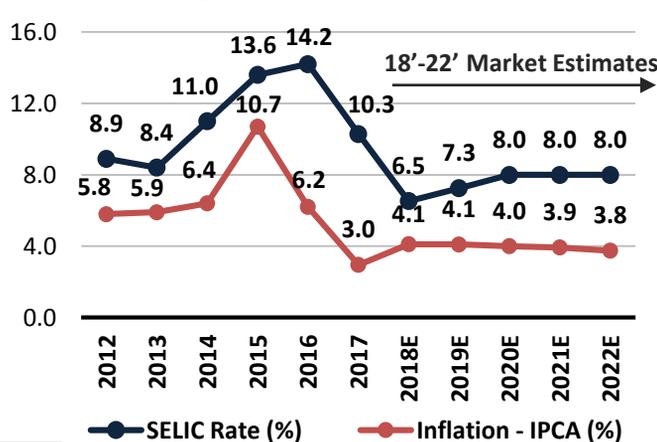
GDP Growth

% Y/Y



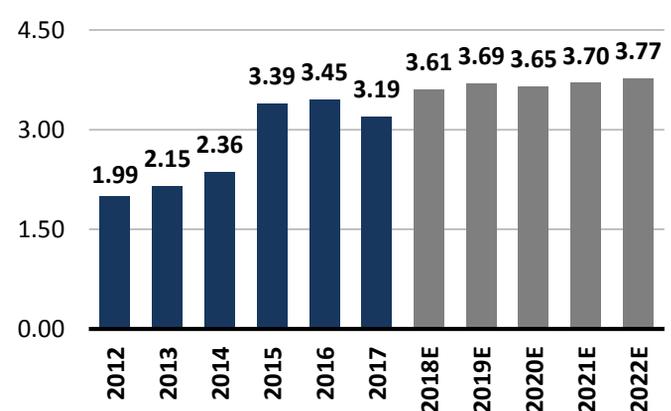
Selic Rate and Inflation (IPCA)

Y/Y %, Year Average Selic Rate



BRL/USD Fx Rate

BRL/USD, Year Average



Sources : Brazil Central Bank (on Aug-18), IBGE, B3-Brazil Stock Exchange

The Gross Domestic Product (GDP) – 1H2018 Analysis

Brazilian GDP rose 1.0% on the second quarter of the year when compared to the second quarter of 2017, consolidating the fifth straight quarter with economic growth after a 12-quarter recession period.

- Although Brazil is **firmly back in economic growth trajectory**, the rate of recovery is increasingly diminishing ahead of the presidential elections in October.
- The slowdown in the first quarter was due to a **deterioration in most components of the GDP**. Fixed investment growth slowed from 3.8% annually in Q4 to 3.5% in Q1, but rose again to 3.7% in Q2, still holding up in a level **well above the past 10 quarters prior to Q4 2017**. Government spending fell 0.8% on Q1 **reflecting fiscal adjustment efforts** (Q4 2017: -0.4% y/y), and remained stable in Q2. On the other hand, private consumption had the **best annual growth in Q1 2018 since Q4 2014**, in all likelihood boosted by the historically **low inflation rates, decreasing private indebtedness and improving consumer confidence**.
- Both exports and imports growth fell in the first quarter. Although helped by **higher commodity prices**, total exports saw a decrease mainly due to **lower agricultural production** and a high base of comparison due to last year's outlier output in Q1, as was severely affected by the trucker's strike in Q2. Meanwhile, **imports grew 7.7% and 6.8% in Q1 and Q2, respectively**.
- Brazil still has **significant issues** to deal with in order to secure **long-term sustainable growth**, such as financial volatility, the negative effects of exchange rate depreciation on inflation (and thus on the ability of monetary policy to stimulate the economy), doubts about whether the next government will face **fiscal problems** and the consequences of the recent truckers' strike, among other factors.
 - This framework made market estimates form GDP growth in 2018 and 2019 decrease from 2,9% and 3,0%, respectively, in May 2018 to 1,5% and 2,5%, in August 2018.
- If the country is able to reduce **exposure to political developments** past the October elections, Brazil has improving factors that should support the continuation of the economic growth in the short and medium terms, such as decreasing individual and corporate indebtedness, inventories in stable levels, increase in hiring, low inflation pressure and solid external accounts.

GDP Composition

% Q/Q-4 growth

	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18
Value Added	(2,7%)	(4,3%)	(5,6%)	(5,2%)	(3,4%)	(2,7%)	(2,5%)	(0,0%)	0,4%	1,4%	2,1%	1,2%	1,0%
Agribusiness	4,3%	(0,1%)	0,6%	(6,5%)	(4,1%)	(3,6%)	(1,8%)	18,5%	14,8%	9,1%	6,1%	(2,6%)	(0,4%)
Industry	(4,8%)	(5,7%)	(8,1%)	(6,9%)	(3,2%)	(2,8%)	(3,0%)	(1,0%)	(1,9%)	0,4%	2,7%	1,6%	1,2%
Services	(2,1%)	(3,4%)	(4,2%)	(3,5%)	(2,6%)	(2,1%)	(2,3%)	(1,6%)	(0,2%)	1,0%	1,7%	1,5%	1,2%
Effective Demand	(2,7%)	(4,3%)	(5,6%)	(5,2%)	(3,4%)	(2,7%)	(2,5%)	(0,0%)	0,4%	1,4%	2,1%	1,2%	1,0%
Consumption	(2,1%)	(3,9%)	(6,1%)	(5,9%)	(4,9%)	(3,4%)	(3,0%)	(1,7%)	0,6%	2,2%	2,6%	2,8%	1,7%
Gov. Spending	(1,6%)	(1,8%)	(2,0%)	(0,4%)	0,2%	(0,3%)	0,2%	(0,5%)	(0,8%)	(0,6%)	(0,4%)	(0,8%)	0,1%
Investment	(12,5%)	(14,9%)	(18,7%)	(17,3%)	(8,6%)	(8,5%)	(5,9%)	(3,7%)	(6,7%)	(0,5%)	3,8%	3,5%	3,7%
Exports	8,6%	2,1%	12,8%	13,0%	3,8%	0,2%	(7,6%)	1,8%	2,5%	7,6%	9,1%	6,0%	(2,9%)
Imports	(11,2%)	(19,9%)	(19,7%)	(21,3%)	(10,2%)	(6,8%)	(1,1%)	9,8%	(3,2%)	5,7%	8,1%	7,7%	6,8%

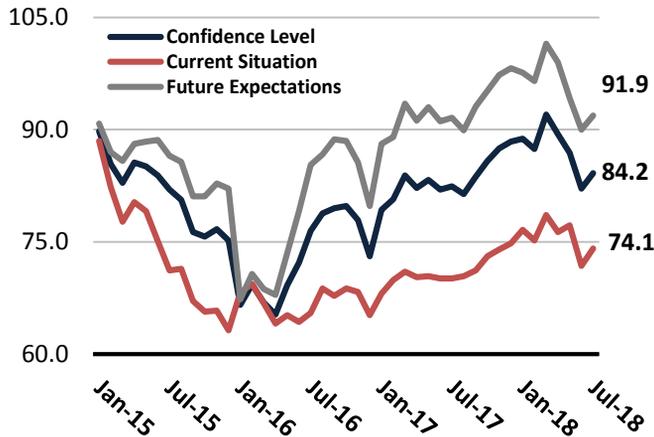
Source : IBGE

Rising Consumer and Industry Confidence

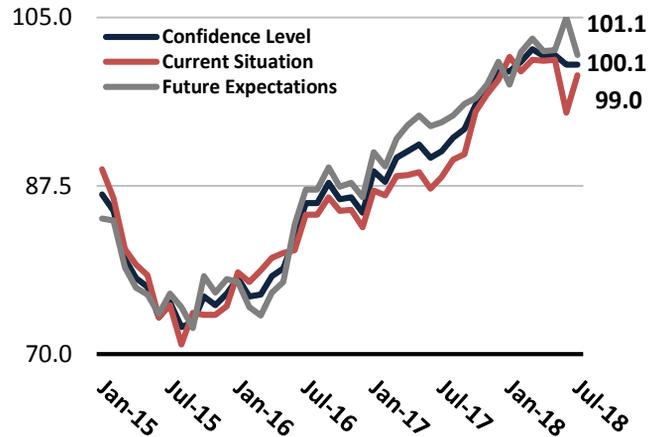
Recent improvements on some activity indicators, such as private indebtedness and net job creation, are positively impacting consumer and industrial confidence indexes, which are slowly rising back to above 100 levels.

- Some other factors supporting short-term economic growth are increasing credit availability for private individuals and companies, historically low inflation and nominal interest rates and industrial inventories at stable levels, among other.
- Political measures approved since 2016, such as the labor and union reforms, contribute to a more pro-business environment, while others such as the new TLP rate (new rate for BNDES loans) and the public spending cap in force reduce long-term investors' uncertainties on Brazil's fiscal sustainability.

Consumer Confidence Index

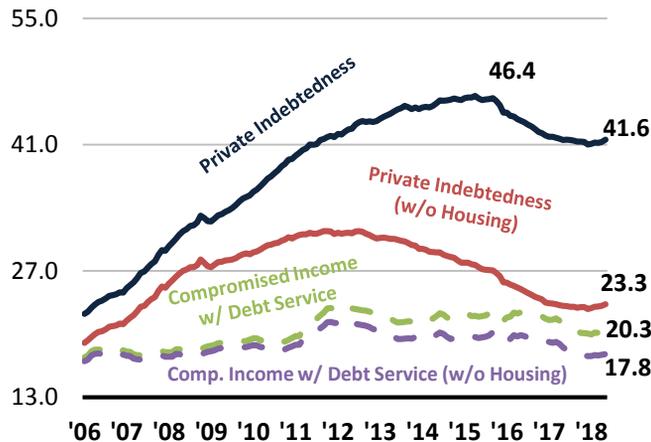


Industry Confidence Index



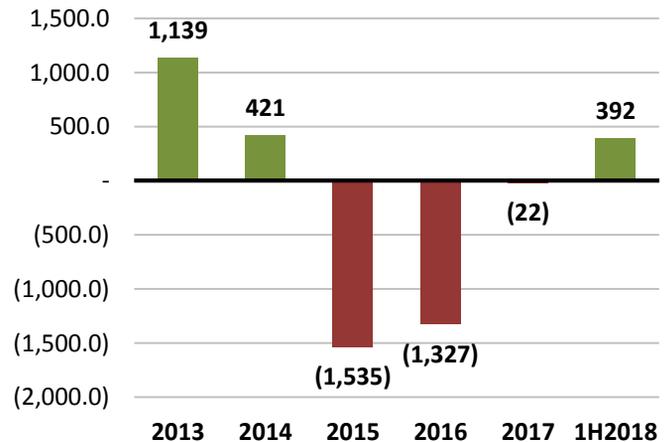
Private Indebtedness

% Total Accumulated Income



Net Job Creation

1,000 Jobs



Source : IBGE, FGV, Bradesco

Brazil Base Nominal Interest Rate (SELIC) and Inflation (IPCA)

On the last Monetary Committee (COPOM) meeting on August 2nd 2018, the target for the SELIC rate was kept at 6.50%.

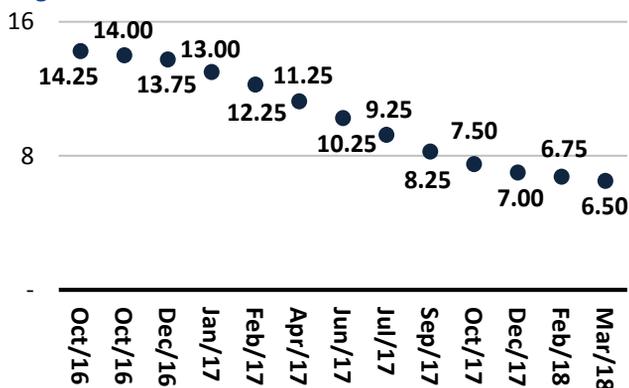
- The target for Brazil’s Base Nominal Interest Rate (SELIC) sits at 6.50% since March 2018, when the Brazilian Central Bank ended a cycle of reductions started in September 16 (at 14.25%).
 - The main reason for the maintenance of the rate at 6.50% was the exchange rate depreciation.
- According to market analysts and consensus expectations gathered by BCB, the goal will most likely remain at 6.50% until the beginning of 2019, when inflationary pressures will force the Central Bank to start a monetary tightening cycle.
- Despite signaling that the SELIC rate should stay at 6.50% until the end of 2018, COPOM faces opposed incentives for the next steps: while a wider output gap, inflation below the target and well anchored inflation expectations favor the maintenance of low rates for longer; sharp currency depreciation (as with other emerging markets) and local political uncertainty significantly deteriorated the balance of risks.

Inflation is at historically low levels, but face risks from political and economic events.

- Inflation in June was at 1.26% m/m, well above the year ago print and the historical norm for the period, reflecting the trucker strike at end-May/early June.
 - This monthly rate increased the 12-month accumulated inflation to 4.38%/y, when compared to an average 2.80%/y in the past 5 months.
 - Nonetheless, the strike’s impacts are already in fast dissipation, as evidenced by the drop in the monthly IPCA-15 (similar to the IPCA, but data is collected in the middle of the month) from 0.64%/m (in July), to 1.11%/m (in June).
- Despite the BRL depreciation and a strong rise in regulated prices presenting a risk to free market prices ahead, anchored inflation expectations and the slow economic rebound should help in curbing these upward price pressures.
- Energy and public transport groups were the main drivers for lower regulated-price inflation (1.3%/m in July vs. 2.4%/m in June), while lower food-at-home inflation led to a decrease in free-market prices inflation (0.7%/m in July vs. 2.3%/m in June).

Previous COPOM Targets for the SELIC

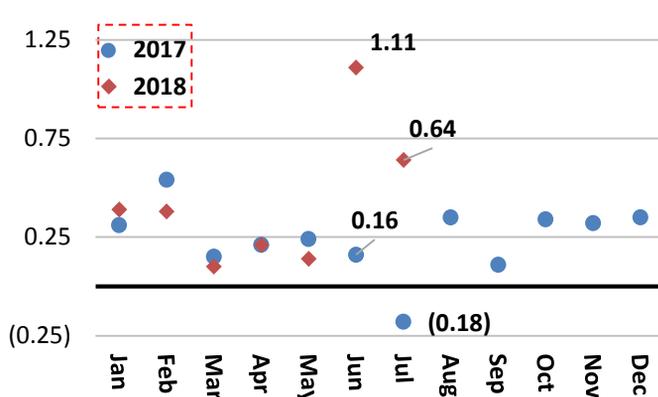
Target SELIC Rate



Source : IBGE, Central Bank

Monthly IPCA-15

% m/m



Key Short-Term and Medium-Term Challenges

Worsening emerging markets financial conditions.

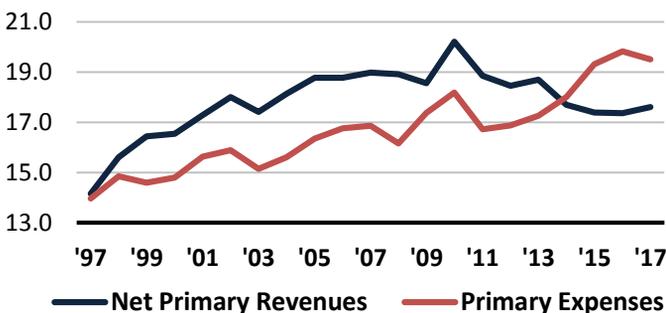
- Various external macroeconomic factors have led to a tightening in EM financial condition. The U.S. economic growth and increase in nominal tax rates, an appreciated Dollar, commercial tensions and lowering of the international commerce due to protectionism policies in various countries and geopolitical tensions in Iran, Syria and Russia, among other factors, reduced appetite for riskier assets.
 - This framework affected Brazil in particular, mostly given the country's fiscal challenges, the uncertainty around economic policy after this year's election and a record low interest rate differential.

Doubs regarding the equalization of the deteriorating public accounts.

- Public debt keeps rising in relation to the GDP, reaching 77.2% in June 2018. Recent tax increases and restrictions on public spending (including the cap for public spending growth in force since the beginning of 2017) have been insufficient to reverse the negative fiscal trends.
- Public expenditure remains high, largely due to the increase in the expenses in which the government has no discretionary power to reduce, as is the case of social security expenses

Public Primary Result

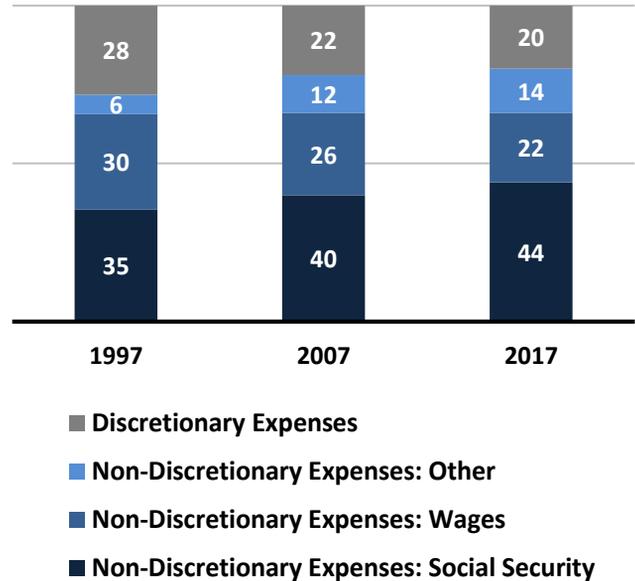
% of GDP



Source: BBVA, Brazil Central Bank

Composition of Primary Expenses

% of Total



Political Uncertainty.

- The race for presidency is still open, with candidates ranging from the far left to the right-wing with chances of winning in October.
- Polls show that a high level of voters' support for "none" or "void", reinforcing the point that the electoral outcomes remains highly uncertain.
- The record-high rejection rate faced by current president Michel Temer also indicates an elevated level of distrust in the establishment.
- Even with a market-friendly outcome, the next government will still face significant challenges in unifying the highly polarized public opinion in order to implement much needed reforms to overcome the fiscal unbalances.

Recent Political Developments and October Elections

Lula Situation and the Worker’s Party Candidate.

- Former president Lula, serving a 12-year sentence for corruption after being found guilty by the appeals court (TRF-4), led opinion polls for the presidential race until September 11th when he was substituted by Fernando Haddad as the Worker’s Party (PT) candidate.
 - Even with his conviction for corruption, Lula still has a large vote recall, specially among the poorer population of Brazil. Polls previous to September 11th showed Lula going head-to-head with Bolsonaro for the lead in vote intentions.
 - Despite the Worker’s Party efforts to enable Lula’s candidacy, he was ultimately substituted by Haddad (the change was made on the judicial deadline for candidacy registration).
 - Since Brazilian law bars convicted criminals to dispute political offices, PT could have ended up with no candidate if they insisted with Lula. The political party hopes for a large amount of votes transferred from Lula to Haddad on election day.

Current Presidential Race.

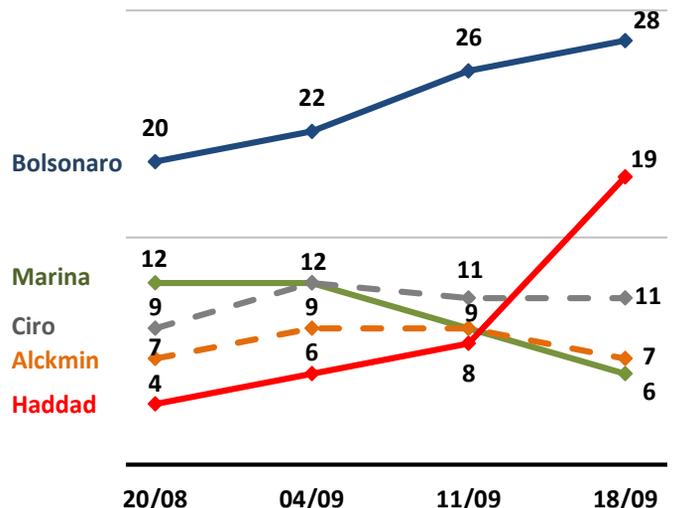
- Right-wing Congressman Jair Bolsonaro, currently hospitalized after being stabbed in an assassination attempt by a left-wing militant, leads isolated with 28% of vote intentions, followed by the Worker’s Party candidate Fernando Haddad (19%).
 - Candidates more aligned with the center of the political spectrum (Marina Silva – center-left, Ciro Gomes – left and Geraldo Alckmin – center) are technically tied behind Fernando Haddad, and are still disputing a spot in the second round of the elections with the Worker’s Party candidate.
 - The low popularity of traditional politicians display the current strong distrust in the establishment by Brazilian voters.
- Center candidate Geraldo Alckmin, who appears with 7% of the vote intentions in the latest IBOPE poll, agreed on coalition with a large portion of Brazil’s center parties on August. This agreement gave him the largest slot in Brazil’s obligatory public television airtime for political candidates, but this advantage did not materialized in vote intentions so far.

Timeline Until the 2018 Elections

July / August	September
August 15 ▪ Deadline for the registry of candidacies.	September 29 ▪ TV & radio campaign ends.
August 16 ▪ Campaign begins.	October
August 26 ▪ TV & radio campaign begins.	October 7 ▪ First round of elections.
September	October 12 to October 26 ▪ TV & radio campaign for the Second Round.
September 11 ▪ Judicial deadline for candidacies	October 28 ▪ Second Round of elections.

IBOPE Election Polls (Top 5 Candidates Only)

% of Total Votes



Recent Political Developments and October Elections (Cont'd.)

Jair Bolsonaro Stabbed in an Political Assassination Attempt.

- On September 6th of 2018, the frontrunner candidate for Brazil's presidency Jair Bolsonaro was stabbed in during a rally in the southeastern state of Minas Gerais.
- Bolsonaro was being carried by supporters and waving to the crowd when the attacker plunged a knife into his abdomen.



Bolsonaro at the moment of the attack

- The candidate was rushed semi unconscious to the hospital, where he underwent emergence surgery. According to medical reports, the knife pierced through his intestines, resulting in severe blood loss.
 - The recovery period will limit Bolsonaro to campaigning only through video during the whole first round (and probably during the second round).
- The attacker, captured on scene by supporters and handed over to the authorities, where he confessed the crime, was discovered to be Adelio Bispo de Souza, a leftist militant and former affiliate of the Socialism and Liberty Party (PSOL).
- Police found four cellphones in the pension Adelio was staying in, and authorities are now investigating if Adelio acted alone or if Bolsonaro's assassination was ordered by someone.

President Michel Temer with Record-High Rejection Rates.

- In recent polls, current president Michel Temer reached a historical record rejection of 82% of the population, making him the most unpopular president in Brazilian history. Unpopular fiscal reforms, the Trucker's Strike and slower-than-predicted economic recovery helped bringing rejection up.

Trucker's Strike

- On the end of May 2018, a major trucker's strike broke out in Brazil, supported by a large portion of the population. Protesters demanded mainly an immediate reduction in diesel prices.
 - The strike escalated to the point of leading to fuel and food shortages in parts of the country.
 - The event has had important political consequences, testing the government's ability to lead in an environment of tough fiscal constraints and reduced political power.
- The government and the Congress responded with tax cuts, fuel subsidies, tolls reductions and market protection for independent truckers.



Highway during the truckers' strike

Financial Markets – 2018 Update on IPOs and M&A Transactions

Initial Public Offerings: starting in strong 1Q2018.

- In the first quarter of 2018, IPO and follow-on volumes in Brazil reached BRL6.9 billion (approx. USD1.8 billion).
 - The amount rose 97% on the first quarter of the year, when compared to the last quarter of 2017
- In total, three operations were carried out in the period, with primary and secondary offerings of shares.
- IPO announcements had been growing strong since 2017, but uncertainties brought by the proximity of the 2018 presidential elections coupled with less international appetite for emerging markets' risk decreased the speed of initial public offerings after 1Q2018.

- The main sectors in terms of number of transactions were Healthcare Services (15), Internet Software and Services (15), IT Consulting and Other Services (13), Application Software (12), Commodity Chemicals (11), Renewable Energy (11) and packaged Foods and Meats (10).
 - In terms of total announced transaction value, main sectors were Paper Products, Electric Utilities, Aerospace & Defense and Education Services, reflecting the largest M&A transactions in this year.
- The recent successful wave of IPOs should contribute to an increase in M&A activity, as re-capitalized companies with stronger balance sheets may consider new acquisitions.

IPOs in 2018 (Sector, IPO Volume)

Successful IPOs – 1Q2018

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Healthcare	Financial Institutions	Healthcare
BRL2,720MM	BRL722MM	BRL3,310MM

Mergers and Acquisitions: major transactions in 1H2018.

- BroadSpan identified 328 transactions involving Brazilian targets in the first half of 2018. Those include M&A, large real estate acquisitions, acquisitions of mining reserves and acquisitions of energy plants and projects, among other.

Largest Announced Transactions in 2018



1. In March 16th of 2018, Fibria and Suzano, the largest two players in the Brazilian short-fiber pulp and paper industry, announced that the two companies would join their operations. The transaction involved Suzano acquiring 100% of Fibria's shares with cash and shares, in an operation that valued Fibria at around USD9.2 billion.



2. In July 5th of 2018, Boeing announced the acquisition of 80% of the commercial aviation division of airplane manufacturer Embraer for USD3.8 billion



3. In June 4th of 2018, Enel announced the acquisition of 73% of energy distributor Eletropaulo for around USD1.5 billion.

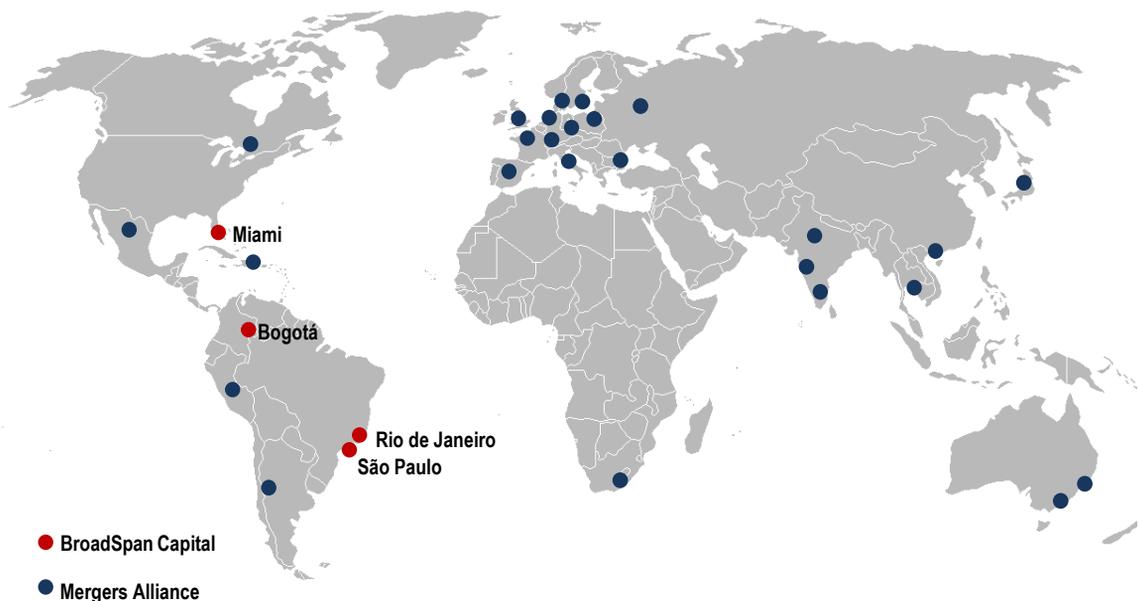
BroadSpan Capital Credentials

BroadSpan is an independent investment banking and asset management firm that specializes in Latin America, the Caribbean and certain segments of the U.S.

- BroadSpan was founded in 2001 with the objective of addressing increasing demand for high quality investment banking services among emerging middle-market companies in Latin America, the Caribbean and the U.S.
- The BroadSpan team is comprised of accomplished professionals who have dedicated their careers to emerging markets and spent many years in major international financial firms.
- With offices in Miami, São Paulo, Rio de Janeiro and Bogotá, along with collaborative agreements in selected markets, the BroadSpan team covers Latin America, the Caribbean and certain segments of the U.S. market across all major industries.

- Complementing its proprietary structure, BroadSpan is the representative of Mergers Alliance for Latin America (ex. Mexico, Peru and Chile). This global partnership allows BroadSpan to offer its clients global reach in the execution of cross-border transactions.
- Additionally, in selected cases BroadSpan has entered into strategic partnerships with global players such as Bank of America Merrill Lynch, Morgan Stanley and Banco Sabadell to provide investment banking expertise regionally.

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Relevant Information

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