

Brazilian economy

Brazil's shrinking GDP fuels recession fears

Latin America's largest economy suffers first-quarter contraction in blow to Bolsonaro



Weakening economic indicators and political infighting have weighed on sentiment in Brazil © Bloomberg

Bryan Harris and Andres Schipani in São Paulo MAY 30, 2019

Brazil's economy shrunk in the first quarter of this year, data on Thursday showed, in a damaging blow to President Jair Bolsonaro and his plans to kick-start growth in Latin America's largest country.

The [development](#) — marking the first contraction since 2016 — has raised fears that Brazil could return to recession less than two years after emerging from a brutal years-long downturn.

More than 13m people in Brazil are currently unemployed, and millions more are underemployed. About 55m people — more than a quarter of the population — now live below the poverty line, up from 52m in 2016.

With investment lagging, much of the [nation's infrastructure](#) and many public services are in decay.

“The picture is worrying and the risk of a recession is concrete,” said Zeina Latif, chief economist at XP Investimentos in São Paulo.

“A central issue . . . is the decline of business confidence as a result of changing signals from the government and the political errors the administration has been accumulating.”

The growing pessimism will be a blow to Mr Bolsonaro, who in October [was elected](#) by mostly middle- and upper-income Brazilians who believed his liberal economic agenda would attract investment and [reignite growth](#) in Latin America's largest economy.

Following the vote, [business optimism](#) jumped and the stock market soared on hopes that Mr Bolsonaro, and his economic team led by minister [Paulo Guedes](#), would pass a crucial [pensions reform](#) widely seen as necessary to restore confidence and spur economic growth.

We don't have a recession — yet. But the economy more or less stopped. It is a very unstable situation

Marcos Lisboa, an economist at Insper business school

But while the reform is still poised to pass later this year, a host of weakening economic indicators, as well as unrelenting [political infighting](#) in Brasília, have begun to weigh on broader sentiment and outlook.

“In this political environment I am just afraid Brasília is going to blow everything up again. I am going to wait until I get a clear signal from Brasília that we are going in the right direction,” said a senior banker in São Paulo.

“People need a higher level of confidence to invest in the real economy.”

On Thursday, official government data showed a contraction in gross domestic product of 0.2 per cent in the first quarter. This follows the release of a host of weakening indicators, including industrial production, down 2.2 per cent in the first quarter, and the overall service sector, which has slowed 1.7 per cent.

Economic growth for the year is now forecast at 1.2 per cent, down from an estimated 2.6 per cent in January, according to the Focus Bulletin published by Brazil's central bank.

“We only see cuts in education and health. Businesses need employees but they are not hiring in order to reduce costs. It is a situation in which social inequality only increases,” said Vanderley Moretto, who has been unemployed since November.

Tony Volpon, chief economist at UBS in São Paulo, attributed the quarterly contraction to “negative shocks . . . like the crisis in Argentina, the global slowdown especially in manufacturing and the [Vale dam disaster](#) in Brumadinho.”

But he pointed out that Brazil was stuck in a “low-growth equilibrium” due to a lack of investment.

“What everyone has been waiting for the last two years is some normalisation of investments, [for investments] to start crawling back to pre-recessionary levels, and that has not happened,” he said.

Much of this corporate reticence stems from concerns over Brazil's precarious fiscal position — a situation Mr Guedes is hoping his pension reform proposal can address.

Battered by a plethora of social welfare obligations, Brazil's fiscal deficit has ballooned in recent years, and gross public debt is forecast to hit 90 per cent of GDP this year, according to the IMF.

"The great drama of Brazil is the accelerated growth of spending, which is underpinned by an unsustainable pensions system," said Marcos Lisboa, an economist with the Insper business school.

"The longer it takes to solve that problem, the longer it will take for the economy to recover, the more fragile the economy becomes and the more sensitive it is to negative shocks."

There are some bright spots, however. Corporate earnings are healthy across many sectors. Reported profits from companies listed on São Paulo's B3 stock exchange last year reached R177bn (\$44bn), up 40 per cent from R125bn the previous year, according to data from Economatica.

In the private sector, there is "clear movement towards growth and investments", said Alvaro Gonçalves, chief executive of private equity group Stratus.

Some economists also believe that GDP growth will pick up in the second half of the year.

"The expectation is for stronger growth, upwards of 0.5 per cent for each quarter. This reflects the dissipation of the clouds of uncertainty, especially in relation to the reform agenda," said Thais Zara, chief economist at Rosenberg Consultants.

However, she added it "depends very much on the political environment and the approval of the pension reform".

Mr Lisboa echoed the sentiment, saying the situation was very precarious.

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Additional reporting by Carolina Unzelte

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