

AUGUST - 2019

MONTHLY STATEMENT

PLANNER REDWOOD ASSET MANAGEMENT

“Brazil is not a country to take seriously”

Popularly attributed to General Charles de Gaulle

Brazil-France relations have a long history, but it has not always been “smooth”. In almost half a century, several episodes had tensions rising, the most troublesome being the last diplomatic incident - known as the Lobster War (1963).

In this past month, French President Emmanuel Macron has once again “jabbed” Brazil, and in a very unfortunate way. Because of the Amazon fires, whose statistics are not yet “pacified” and properly adjusted to what really matters, Macron suggested, with his phrase “our house is burning...”, raising the issue at the G7 meeting. Mincing with words aside, a blatant intrusion into our sovereignty – an ages-old idea of defining an international status for the Amazon. The effect could not have been more immediate: President Bolsonaro, in his best non-diplomatic style, responded right away.

The episode is likely to quickly dissipate, but Bolsonaro insists on a recant by the French president. Obviously this a flashing subject for the international press, and may have some economic impact for Brazil. However, given the global economic predicament, it is unlikely that this agenda will gain relevance as compared to other problems around the world. In any case, apart from the back and forth, in the face of an unwarranted provocation, Bolsonaro is quite correct in demanding retraction.

The long history between the countries does not allow for rising tensions, not even our companies and huge chain of trade would yield to such shameless and misleading a statement (possibly for political ends). It will only be a matter of time before the real diplomats know

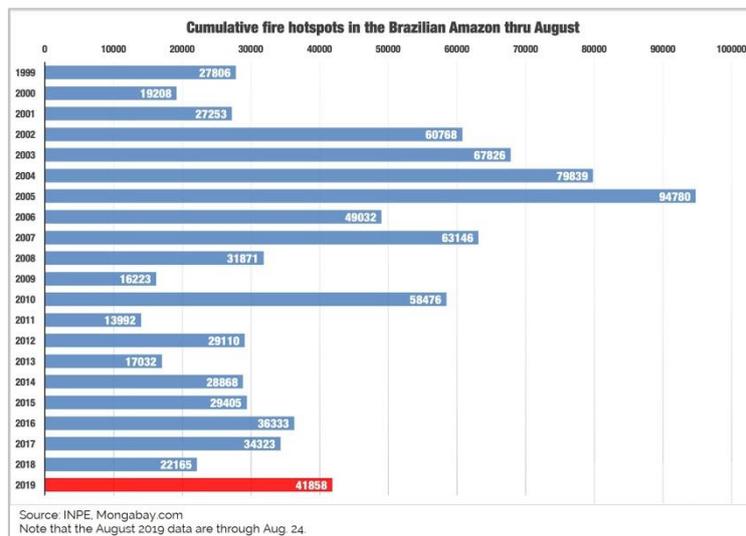
how to bring order to this mess.

Indeed, this “crisis” has gained ground for a number of reasons, including the environmental “fever” (with no disparage) that strikes the world, Macron’s internal political situation with sectors that could take advantage of any consequences of this “crisis” and, not least, the “new normal” that is spreading around the world, in which the current Brazilian government is inserted. Thus, although the quote in the epigraph is attributed to Gal. de Gaulleⁱ, it seems unlikely that he actually mentioned it, because albeit a difficult person (strong background and temperament), he was very polite. Admittedly, Macron, also polite and intelligent, will recant from his statement, otherwise the subject of the above sentence will be reversed.

In the markets, some indicators had a significant reversal in August. Although the Ibovespa closed down with -0.67% at 101,135

points, it touched the low level of 95,855 points on Aug 27. Interest rates DI1F20 and DI1F21 did not swing significantly (as well as the rest of Yield Curve), closing the month at 5.41% and 5.53%, respectively. Brazil risk, as measured by the 5-year CDS, rose 8 points, closing the month at 134 points. The Dollar (Ptax) ended the month at BRL 4.1385, an increase near 10% in the month, due to international and domestic issues - a phenomenon of devaluation that impacted several currencies in the world (developed and emerging), but with important intensity in the Real.

The recent result of economic activity, though small, has been a relief to the specter of a “technical recession,” but is merely a “Mona Lisa smile”. Timidity aside, the reaction is far from being consolidated, let alone



MONTHLY STATEMENT

AUGUST - 2019

structured in any way. We are far below potential, and the understandably sluggish economic recovery frustrates everything else from it. We have depended for a long time on government investment, and this reality no longer exists, so the ability to resurrect private investment will take some time.

Corroborating the above analysis and all the information discussed last month about the GDP of the Industry, July results for manufacturing output on the previous month are as follows: a 0.3% drop against an expectation of a 0.45% increase. Compared to July 2018, output fell 2.5%. In 2019, manufacturing fell by 1.7% and, in the past 12-month period, the industry's production accumulated a 1.3% decrease. The industry operates 18.3% below its peak output score in May 2011. Truly a disaster!

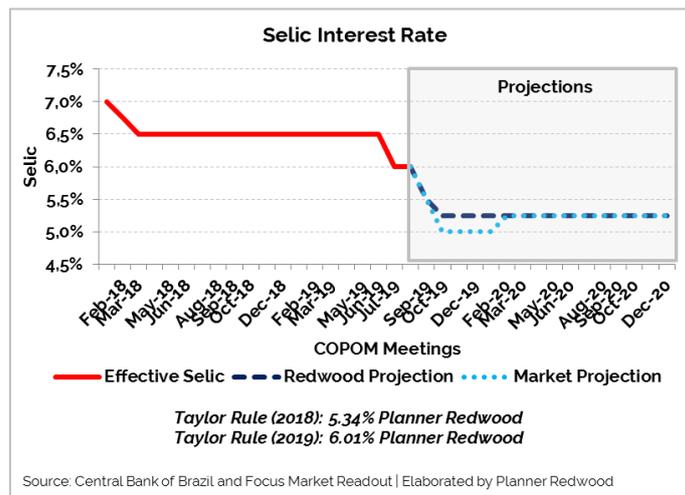
And it doesn't stop there: the production of capital goods also fell 0.3% in July when compared to June. From another perspective, the industry recorded output losses in 11 of the 26 surveyed activities from June to July. The extreme point of the analysis is that if this behavior of manufacturing activity carries on for long, the cumulative effects of this situation could do away with the national industry and its eventual reconstruction will cost much time and effort.

The good news (perhaps) is that despite these poor official August figures, the expectation is that the Brazilian economy should resume its recovery path starting in September. Why is that? Because while the second half of the year started a little "shaky", other data are mixed, such as better confidence and credit indexes, with rising consumption (0.8% margin) and falling unemployment, both contributing to some positive effect. In addition, other indicators in Brazil are faring well, not to mention our "comparative" advantage over prospective international scenarios.

In parallel, the economic team is studying ways to exempt companies from payroll taxes in order to encourage employment. In other words, what the economic team wants is for tax reform to help boost job creation in the country. It is a program to relieve companies from paying payroll taxes when hiring young people and people who have been outside formal labor markets for more than two years. It would be a wide exemption of payroll taxes, as a way to boost job creation in the country. We need more information to give a proper opinion (any initiative in this field is welcome), but we warn of its ineffectiveness and even scope for "arbitration" by companies if the program crams in it to many details and restrictions.

The COPOM minutes following the latest monetary

policy decision with the SELIC cut of 0.5% seem to indicate that the next meeting, to be held on Sept. 18, will result in continuity of an easing monetary policy. It does not seem likely to us, however, that this movement will keep its pace in subsequent meetings. There are my reasons for that, but mainly because



BACEN needs some time to evaluate the various variable trajectories underlying its understanding in order to pursue its policy, and the impacts of these variables respond to various lag lengths. This "lag" cannot be short cut, otherwise it will not only frustrate the expected results, but also compromise Bacen's main asset: its credibility.

Regarding the fiscal numbers, few changes were observed in the last 30 days. The ratio of primary deficit to GDP remained at around 1.35% for 2019, while for 2020 it was 1%. The nominal deficit, also in relation to GDP, was 6.20% and 5.99%, respectively for this year and 2020. The surprise, however, now lies in the divergent ideas between the economic team and the government's

political wing as to the convenience of changing the Expenditure Cap rule. As absurd as it sounds, this ghost has returned, and instead of addressing administrative reform, it raises the possibility of "shortcuts." Tackling difficulties due to lack of resources – one needs to understand – must not rely on going around the Expenditure Cap. The way is to have a State that is less costly to society, and yes, even if the government can reduce expenses and even increase revenues, the Expenditure Cap may still be a constraint on investments in governmental works and programs. It is the result of what we have built in recent years – unfortunately. We cannot risk increasing spending, debt, and having a new crisis, throwing away every effort made up to now.

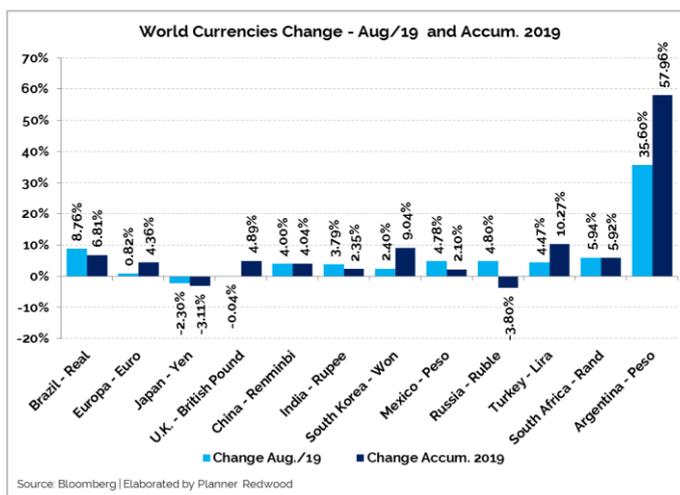
The Brazilian financial markets that performed positively with the wave of "optimism" until July, has cooled and "bent" its knees in August, at least momentarily. The yield curve that had been showing successive downward shifts and negative slope for some maturities have now reversed and/or smoothed this movement. Nothing that changes the pricing landscape, especially for the short term, but clearly a "technical" stop that depends on internal and external factors to continue its movement.

In the stock market, the main stock index, the Ibovespa, ended the month in slight retraction, but had significant swings, touching a floor of 95,855 points in BRL and 23,058 in USD. Foreign investors have definitely not returned, and caution remains. Anyway, with lower real interest rates, extreme international liquidity and the fact that Brazil and other emerging markets are identified as *anti-cash*, the Brazilian stock market should not be overlooked – even though it was one of the worst investments of the month, especially if one has any expertise in stock selection.

The foreign exchange market this month was quite busy. First, BACEN took an important, courageous and technically appropriate attitude: after long years, it decided to intervene in the spot market – especially when the market becomes dysfunctional. The mere mention of the measure made the Brazilian currency, on the following day, behave differently from other currencies around the world. However, the international environment acted strongly in the opposite direction, sponsored by Minister Guedes's statement, a few days after the announcement by BACEN, that "Brazil is prepared for a USD at BRL 4.10 or BRL 4.20". In doing so, he sealed – albeit temporarily – the fate of the domestic currency.

Overseas, markets are in turmoil. Fears of the global recession lead central banks to ease their monetary policies. In China, the PboC has again strongly intervened in the market, and rumors are mounting that Chinese companies are finding it difficult to meet their financial obligations. In the United Kingdom, BREXIT takes an even more dramatic turn in its search for a "peaceful" solution and the country remains in suspended animation for

almost 3 years. In the US, the Fed signals that it will not be as dovish as the market expects, and strongly impacts capital flows around the world. On our nearby shores, Argentina has gone bankrupt. The indication that the left may return to power in the forthcoming presidential elections has obliterated its survival. A pity.



ⁱ Rumor has it that the statement was done by the Brazilian ambassador Carlos Alves de Souza.

MONTHLY STATEMENT

AUGUST - 2019

planner 
Redwood

DISCLAIMER

This material has been prepared by Planner Redwood Asset Management Administração de Recursos LTDA. (Redwood) and is for information purposes only and does not constitute a recommendation for investment, offer or solicitation of an offer to acquire securities or any financial instrument. The information, opinions, estimates and projections refer to the present date and may contain information about future events and these projections / estimates are subject to risks and uncertainties related to factors that exceed our ability to control or estimate accurately, such as market competitive environment, fluctuations of currency value and inflation, changes in regulatory and governmental entities, as well as other aspects that may differ materially from those projected without prior notice. The information herein contained is based on the best available information collected from public, official or credible sources, which we believe to be reliable and of good faith. However, they have not been independently verified and, neither express nor implied warrant is given as regards their accuracy. We are not responsible for any omissions or errors, and even as we have taken all precautions to ensure that the information contained herein is not false or misleading, Redwood is not responsible for its accuracy or completeness. The opinions expressed solely reflect our opinions at the moment. We reserve the right at any time to buy or sell such securities. These projections and estimates should not be construed as a guarantee of future performance. Redwood undertakes no obligation to publish any revisions or update such projections and estimates in light of events or circumstances that may occur after the date of this document. This material is provided for the exclusive use of its recipients and its contents may not be reproduced, redistributed, published or copied in any form, in whole or in part, without the express permission of Redwood.

©2019 Planner Redwood Asset Management Administração de Recursos LTDA. All rights reserved.



planner 

Redwood

Avenida Brigadeiro Faria Lima, 3900 - 10º andar
São Paulo - SP | CEP 04538-132
+55 (11) 2172.2600
planner.com.br