

Highlights

- **GDP growth reached 1% in first quarter, but without support from domestic demand, recovery will remain uncertain.**
- **Meeting expenditure ceiling will require a broad reform of public spending, beyond social security.**
- **Federal government posted a deficit of R\$3.8 billion until April, meeting the target for the period.**
- **Non-recurring revenues helped to reduce frozen discretionary expenditures in R\$3.1 billion.**
- **Public debt maintain its upward tendency, with no prospect of reversing it until 2023.**

Summary

- GDP growth in first quarter was driven by agriculture, while **consumption and investment are still falling**. Economic backdrop has not improved and the risk of a more pessimistic scenario increased. In the face of uncertainties regarding the approval of structural reforms, we ran a simulation of three scenarios for macroeconomic variables which scales the current fiscal challenge.
- **Public sector primary surplus is expected to occur only by 2022, in our optimistic scenario**, which includes the adoption of a mandatory spending reduction program, far beyond social security reform. In this scenario, public sector will have operated for eight consecutive years, from 2014 to 2021, with negative primary balance. Sustainable recovery of primary balances will be particularly slow.
- In the first four-month period, there was R\$19.4 billion¹ in revenue frustration, compared with the government expectation. In order to achieve the fiscal target for the period, spending cuts and other additional constraints, reduced outlays in R\$21.3 billion, which allowed the **federal government to reach the fiscal target (-R\$18,6 billions)**. At the same period, **effective primary deficit was only R\$3.8 billion**.
- Government report for the second bi-monthly budget update unfroze **R\$3.1 billion (from R\$42.1 billion to R\$39 billion) in discretionary expenditures**. From the revenues side, we highlight the increase in concessions and permissions (+R\$7.0 billion), royalties and special fees (+R\$2.0 billion) as well as nontax special installment (+R\$3.4 billion). Mandatory expenditures, in turn, increased R\$3.7 billion.
- **Gross debt continues breaking monthly records**. Since the end of 2013, it has raised more than twenty percentage points of GDP. Despite that trend, we can't **notice notorious evidence on the deterioration of the refinancing conditions or the assumption of new debt in bond market**, in terms of duration and costs. We note that the share of Selic indexed bonds has increased through.
- Gross debt, currently at 71.7% of GDP, may evolve into quite distinct levels in the coming years, depending on the macroeconomic assumptions, notably the **public sector primary balance**. Underlying the primary balance path, are hypotheses about the progress of **tax reforms**. In the baseline scenario, **the debt will fall only by 2024, after peaking 92.4% of GDP**.

¹ Exchange rate on 2017.06.14: R\$ 3.29 per US\$ 1.00.