

Highlights

- **Economic activity data showed moderate expansion throughout the fourth quarter.**
- **External accounts conjuncture remains favorable, on the whole.**
- **Fiscal adjustment stabilizes primary deficit in the short term, but is insufficient to control debt.**
- **Mandatory spending smaller forecast allows unfreezing R\$5 billion¹ in December.**
- **2018 Budget already needs spending cuts.**
- **Brazil has, at present, a broad set of fiscal rules.**
- **Recent estimates of the output gap in the Brazilian economy vary from -3% to -8% for 2016.**

Summary

- Economic activity shows **gradual expansion** in the fourth quarter. In the **labour market**, signs of reactivation can be seen by the **overall wage expansion**, but **employment** progress is determined by categories without formal ties. ([Page 5](#))
- **External accounts evolve favourably**, with the generation of high trade surpluses, which keep the current accounts deficit in low level. This fact, along with **high direct investments**, ensure external funding for the country, in spite of the negative flows of other foreign investments. ([Page 8](#))
- **Positive surprises** around the volume of atypical recipes and incipient reaction of tax collection related to economic activity benefit the performance of **primary revenues**. This fact, along with the **reduction** of subsidies, discretionary spending and PAC investments, has enabled **conjunctural stabilization of the primary deficit** but is insufficient to prevent the rise of public debt. ([Page 19](#))
- **Expectation of a reduction in mandatory expenditure (R\$4.4 billion)** and expected revenue almost stable (decrease of \$0.9 billion in gross revenue and increase of R\$0.4 billion in net revenue) as compared with November report, allow **new spending unfreezing, of R\$5 billion**. With that, blocked spending fall to R\$19.6 billion in 2017. ([Page 22](#))
- **The R\$6 billion loss** concerning the taxation of special funds and the uncertainties regarding the postponement of the rise in public employees wages (R \$4.4 billion) and the privatisation of Eletrobras (R\$12.2 billion) are sources of concern for the implementation of the 2018 Budget, partially mitigated by lower impact of minimum wage in public accounts (R\$3.4 billion). ([Page 24](#))
- Brazil has a **broad set of fiscal rules**, which differ in terms of its object (expenditure, revenue, balance or debt), defining statute (Federal Constitution, law or resolution) and federative scope. Getting to know this set is the first step to discuss how these rules relate to each other and how they can ensure fiscal sustainability. ([Page 27](#))
- After the period of severe recession, from mid-2014 to the end of 2016, estimates for the **output gap** in the Brazilian economy began to show **substantial disparities**, indicating a high degree of uncertainty surrounding the various methodologies. ([Page 30](#))

¹ Exchange rate on 2018.01.12: R\$ 3.21 per US\$ 1.00.