BBVA Research

JUNE 2025

Brazil Economic Outlook

Global economy: main messages

Economic uncertainty

US tariffs have risen sharply. Although levies on China are now around 30%, lower than the expected 60% and well below the post-"Liberation Day" peak of 145%, they remain historically high and the uncertainty about where they will eventually settle is a persistent source of risk. In this context, and given prospects of large fiscal deficits, the US premium risk has risen. Growth remains resilient and inflation has eased, despite early signs of tariff-related deterioration.

Growth outlook

Protectionism and uncertainty will weigh on economic activity. Growth will likely slow more than previously anticipated in the US, but not necessarily in China and the Eurozone. In China, lower-than- expected US tariffs back an upward revision of growth forecasts. In the eurozone, the impact of expected US tariffs will likely be mitigated by fiscal spending, mainly in defense.

Inflation and rates outlook

Tariffs are likely to push US inflation higher, prompting the Fed to keep rates unchanged for longer. Monetary easing could resume by the end of 2025 if price pressures prove transitory. The rate-cutting cycle could be over, or at least near to the end, in the Eurozone, and remains underway in China.

Risks

Lingering policy uncertainty and rising US risk premium are important sources of concern. Tariff risks have augmented, but now appear more balanced.

Brazil: main messages

Economic activity

Growth is forecast to slow to 2.2% in 2025 and 1.6% in 2026, down from 3.4% in 2024. Economic activity exhibited strength in 1Q25, supporting an upward revision of the forecast for 2025. However, tighter economic policies and a less supportive global environment are likely to weigh on growth, particularly in 2026, when it is expected to fall short of earlier forecasts

Inflation

Inflation is expected to gradually ease, reaching 5.0% in Dec/25 and 4.0% in Dec/24. On top of the expected softening of domestic demand, inflation should also be helped by lower commodity prices and a stronger Brazilian real.

Monetary policy

The tightening cycle is mostly over. Although an easing cycle may begin at the end of this year, the Selic rate will likely remain above the estimated neutral level of around 10%.

Fiscal policy

Fiscal risks persist, as structural problems remain unaddressed and the government's commitment to consolidation is still uncertain. Still, the most likely scenario is a waning fiscal impulse, compliance with adjusted targets, and avoidance of a fiscal crisis.

Research

Global Outlook

Global economy under pressure by US policies

High US tariffs; although lower on China, they are larger than assumed on others, and a greater source of uncertainty

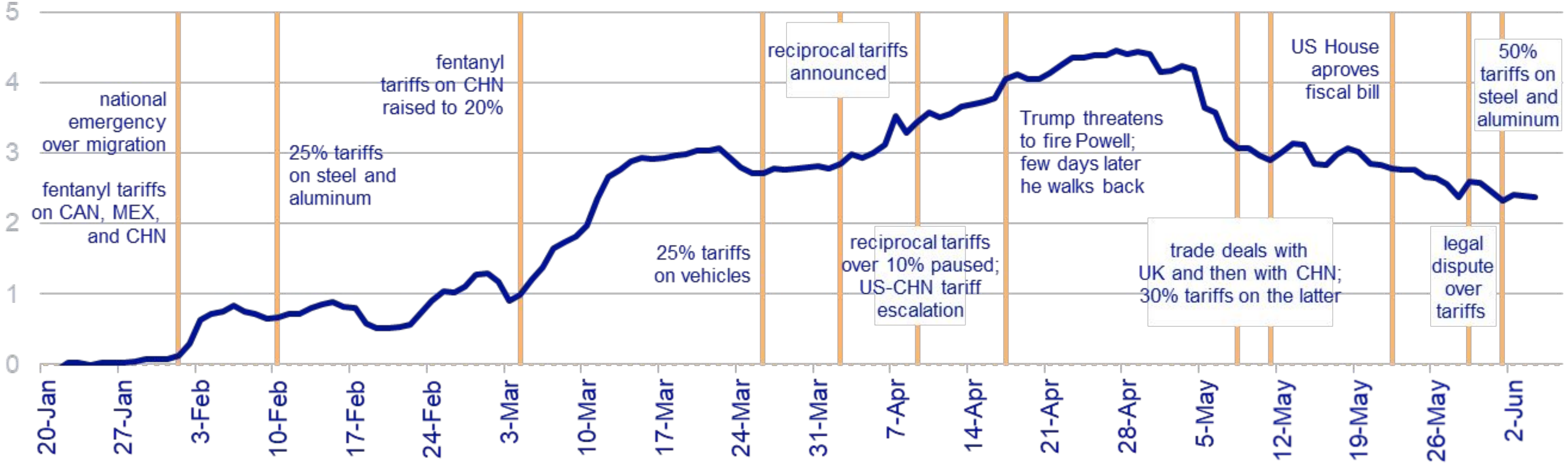
Resilient growth; confidence deteriorated, but impact of tariffs on activity and inflation is limited, so far

Larger US risk amid increasing concerns on fiscal accounts and uncertainty on US policies

Weaker USD, higher long term yields, and a cautious Fed; policy rates fell further in China and Europe

Uncertainty remains in place

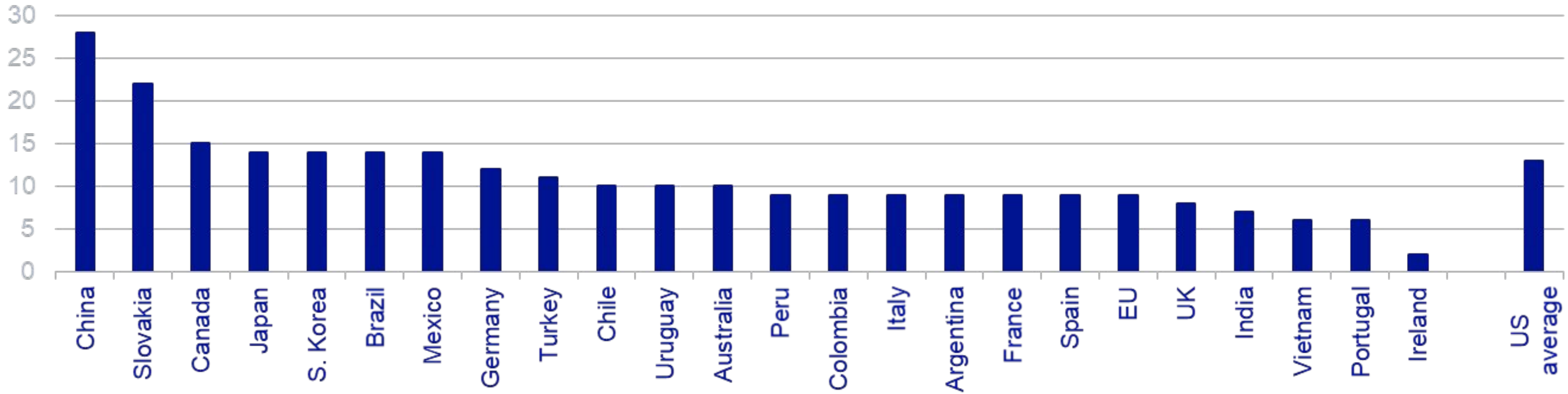
BBVA RESEARCH ECONOMIC POLICY UNCERTAINTY INDEX: UNITED STATES (*)
(28-DAY MOVING AVERAGE, AVERAGE SINCE 2017 EQUALS TO ZERO)



(*) Last available data: June 4, 2025
Source: BBVA Research.

US tariffs have risen sharply and erratically

US TARIFFS: ESTIMATED INCREASE SINCE THE BEGINNING OF 2025 UNTIL JUNE 9, 2025 (*)
(PP)

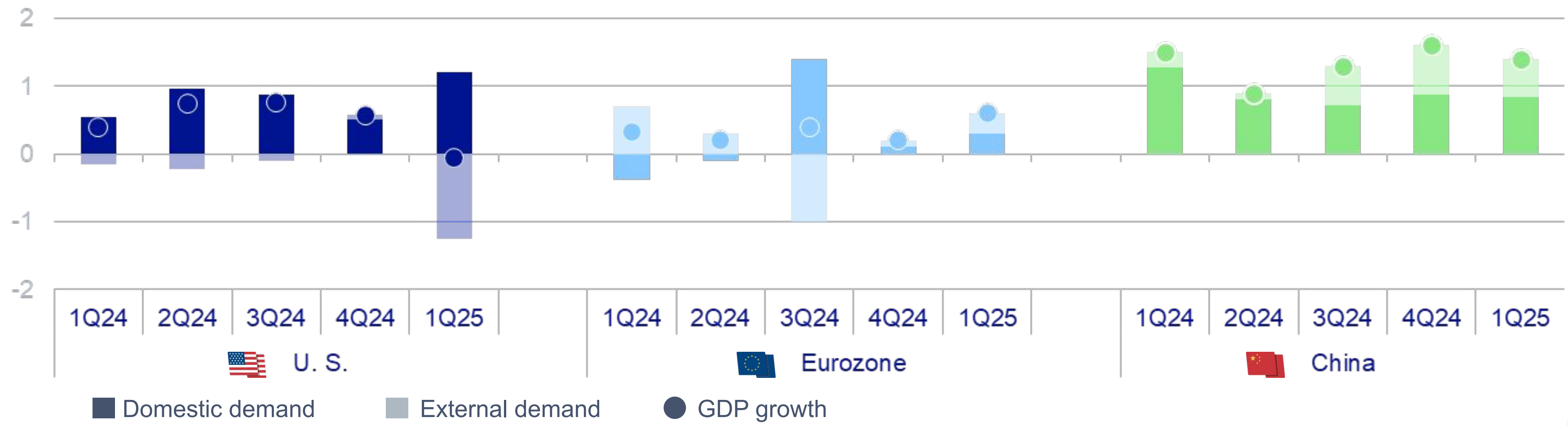


(*) Based on i) 25% tariffs on vehicles and vehicles parts and 50% tariffs o aluminum and steel (lower rates for the UK, Mexico and Canada), ii) 0% tariffs on pharmaceutical goods, oil, copper and selected electronic goods, iii) fentanyl tariffs on China, Mexico and Canada, and iv) 10% reciprocal tariffs.
Source: BBVA Research.

After some de-escalation, US tariffs rose again in late May/25, with levies on steel and aluminum reaching 50%; trade negotiations continue, and disputes over the legal validity of the tariffs remain unresolved

GDP stagnated in the US and grew by more than expected in the EZ and China in 1Q25 amid preemptive trade flows

GDP: CONTRIBUTION OF DOMESTIC AND EXTERNAL DEMANDS TO GDP GROWTH
(GDP GROWTH: Q/Q%; CONTRIBUTIONS TO GDP GROWTH: PERCENTAGE POINTS)

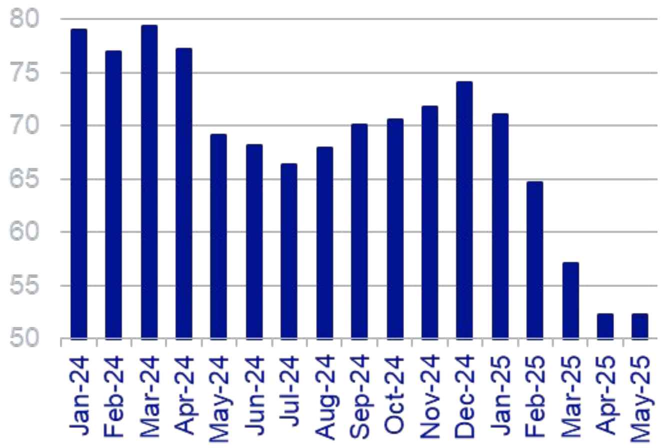


Source: BBVA Research based on data from Haver and China's NBS.

Ahead of tariffs, imports and inventories increased sharply and private consumption weakened somewhat in the US; exports performance helped to sustain growth in China and the Eurozone

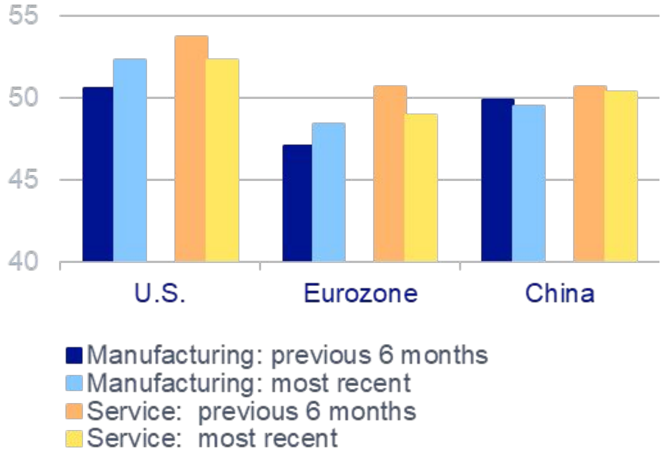
Growth remains relatively resilient, but there are incipient signs of tariff effects on activity

US CONSUMER SENTIMENT
(INDEX)



Source: BBVA Research based on data from Survey of Consumers, University of Michigan

PMI INDICATORS: 2H24 AVERAGE AND MOST RECENT DATA (*) (MORE THAN 50: EXPANSION; LESS THAN 50: CONTRACTION)

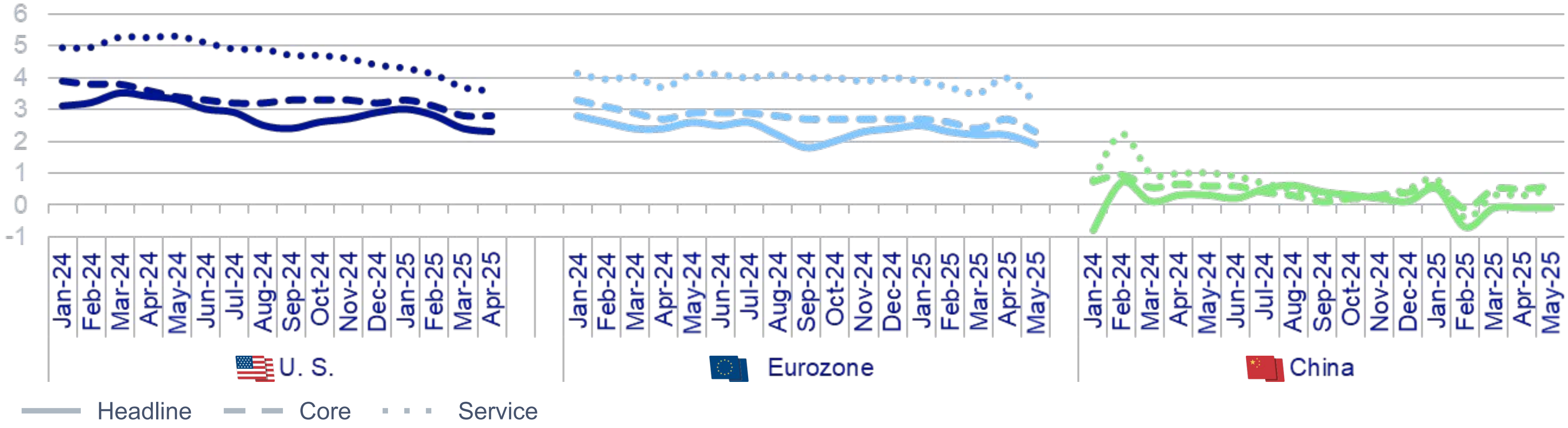


(*) Most recent data: May 2025.
Source: BBVA Research based on data from Haver.

Confidence has deteriorated and services have weakened, while manufacturing has benefited from lower interest rates and pre-tariffs trade surge; labor markets are losing some of their steam, but remain strong

Inflation has eased more than expected lately; limited effects of tariffs so far

CPI INFLATION: HEADLINE, CORE AND SERVICE
(Y/Y %)

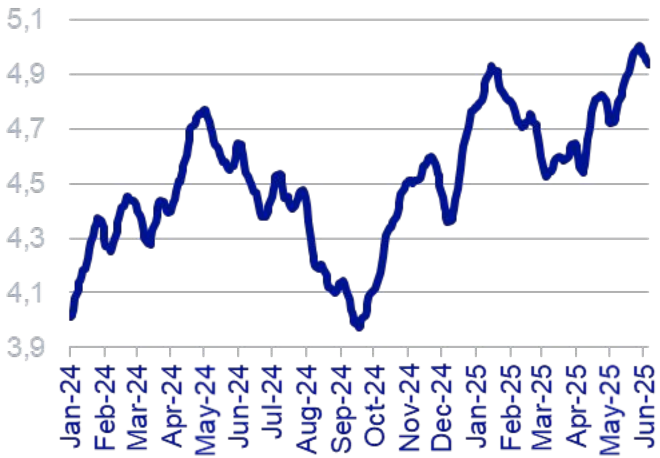


Source: BBVA Research based on data from Haver.

Contained demand pressures and lower energy prices have contributed to a moderation in inflation, which remains over 2% in the US (but not in the Eurozone anymore), to some extent due to still pressured service prices

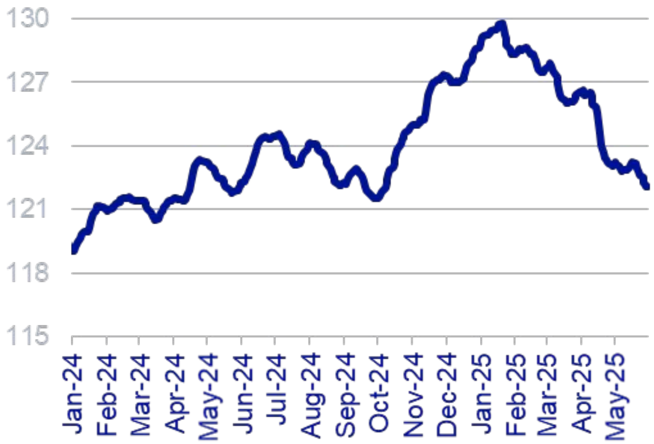
The US risk premium has edged higher, weighing on long-term yields and the dollar

YIELDS ON US 30-YEAR SOVEREIGN BONDS (*) (%, 7-DAY MOVING AVERAGE)



(*) Last available data: June 5, 2025
Source: BBVA Research based on data from the Fed

NOMINAL BROAD US DOLLAR INDEX (*)
(INDEX: JAN/06=100; 7-DAY MOVING AVERAGE)

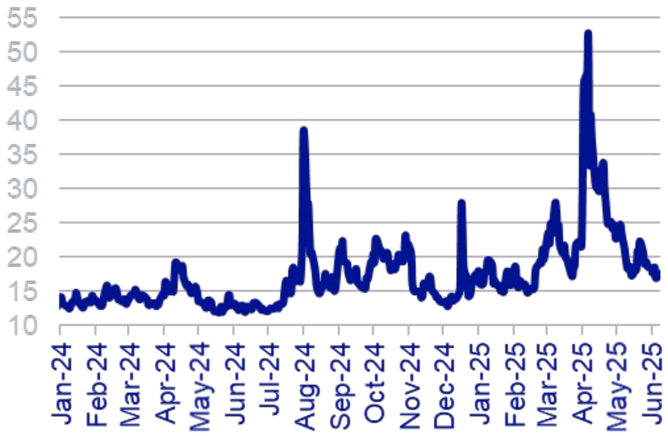


(*) A weighted average of the foreign exchange value of the U.S. dollar against currencies of a broad group of major U.S. trading partners. Last available data: May 30, 2025
Source: BBVA Research based on data from the Fed

Policy uncertainty, prospects of larger fiscal deficits, threats to the Fed independence, talks about a dollar devaluation, a potential tax on foreign investors, among other factors, have pushed US risk up

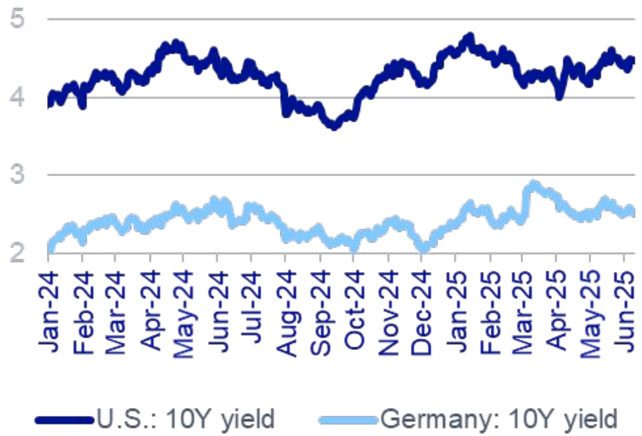
Financial volatility has eased more recently, after having surged in April, but remains elevated

EQUITY VOLATILITY: VIX (*)
(%)



(*) Last available data: June 9, 2025
Source: BBVA Research based on data from Haver

SOVEREIGN YIELDS (*)
(%)

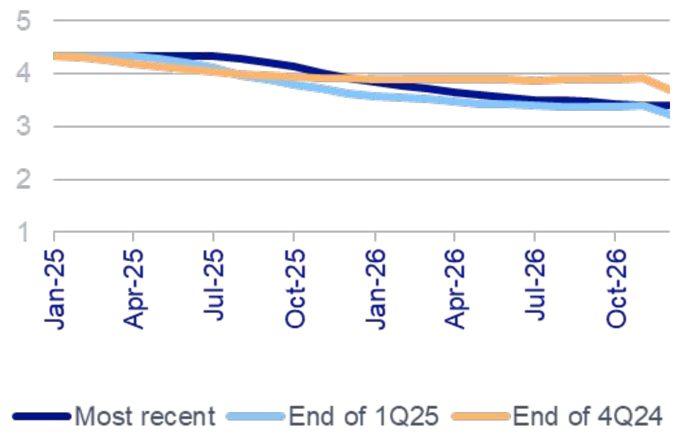


(*) Last available data: June 9, 2025
Source: BBVA Research based on data from Haver

Upward pressure on 10-year sovereign yields due to rising risk premium in the US and fiscal spedning prospects in the EZ, to some extent offset by growth concerns, mainly in the Eurozone

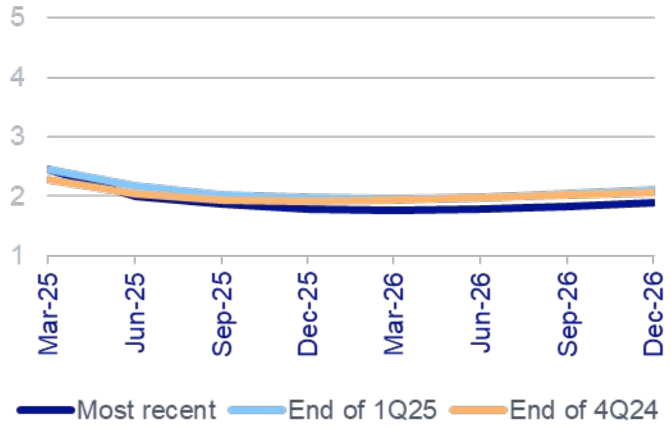
Despite lower inflation, the Fed remains cautious and markets see limited room for extra easing in the short run

US: IMPLICIT RATE IN FED FUND FUTURES (*)
(%)



(*) Last available data: June 9, 2025
Source: BBVA Research based on data from Haver

EZ: IMPLICIT RATE IN EURIBOR FUTURES (*)
(%)



(*) Last available data: June 9, 2025
Source: BBVA Research based on data from Haver

The likely impact of tariffs on inflation has backed the Fed's decision to keep rates unchanged lately; the ECB cut rates to 2% in Jun/25 and suggested that, despite large uncertainty, the easing cycle is nearly over

Base scenario: protectionism and uncertainty will hit the global economy; stimulus will support China and Eurozone

Growth will moderate, faster than forecast in the US although tariffs may be lower than expected; policy stimulus will support China and Europe

Inflation is set to rebound in the US, at least in the short-term, thanks to higher tariffs; it will be around 2% in the Eurozone and low in China

A cautious Fed will keep rates on hold through year-end; ECB's easing cycle is likely over, but extra cuts are dependent on tariffs

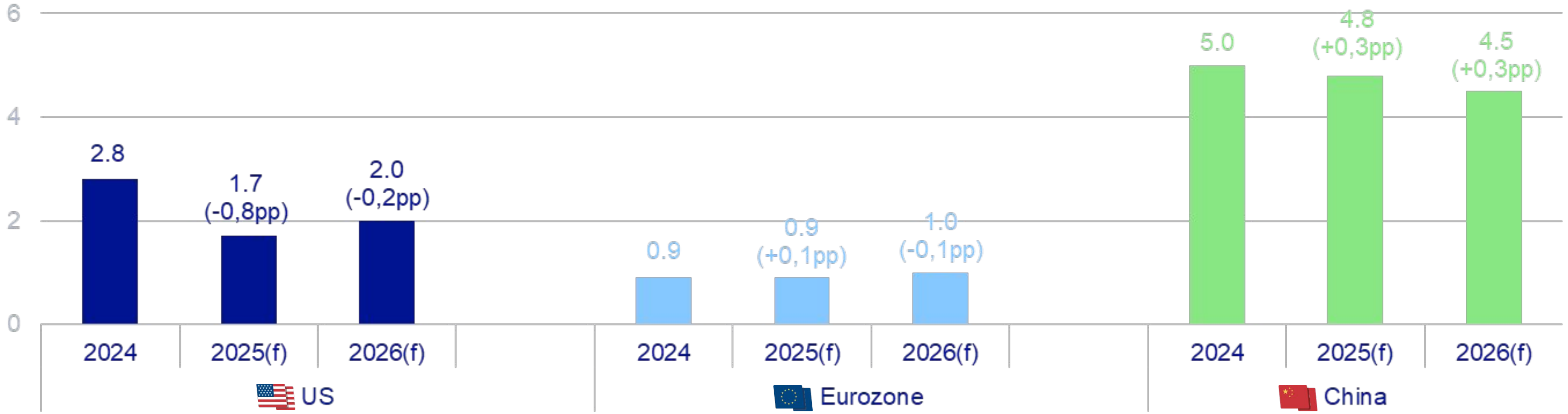
Market volatility will likely persist amid lasting uncertainty and rising US risk, potentially hitting the dollar

Prospects for US policies: baseline scenario assumptions

	BBVA Research baseline scenario on main US policies
Tariffs	**Higher for longer uncertainty, although lower levies on China would imply smaller US average tariffs than anticipated**. Working assumption: around 30% on China, 10% on Mexico/Canada, average of current (as of end of May) and reciprocal (as of “Liberation day”) tariffs for others, implying a 13pp increase in the overall US tariffs (vs. 60% on China and 10% on others, which implied a 17pp increase in US tariffs, assumed in 1Q25).
Fiscal Policy	**Potentially larger fiscal deficits**, driven by significant tax cuts and limited offsetting revenue, will likely weigh on US yields and the dollar.
Monetary and FX Policy	**Higher-than-expected noise** will help keep market volatility and US assets under pressure. Still, the Fed is expected to maintain its independence, and the dollar should remain the dominant global reserve currency.
Other policies	**Migration policies will not have a significant impact on labor markets** in the forecast horizon. No shocks related to foreign and regulatory policies are being assumed.

Growth prospects have deteriorated in the US, but not in China or the Eurozone

GDP GROWTH (*)
(%, CHANGE WITH RESPECT TO PREVIOUS FORECAST IN PARENTHESES)

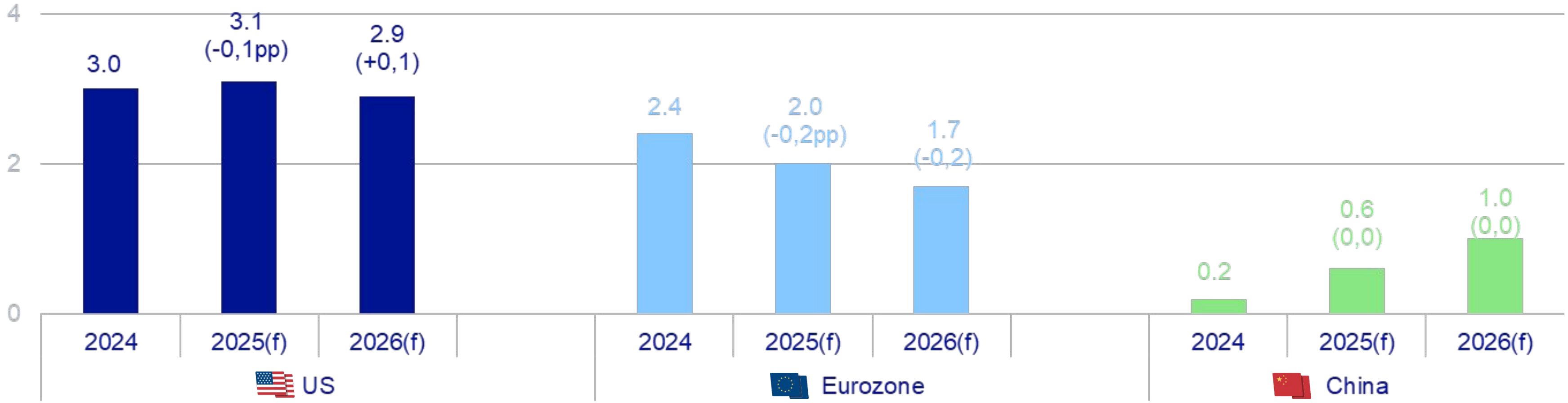


(*) Global GDP grew by 3.4% in 2024 and is forecast to expand by 3.0% in 2025 and 3.1% in 2026, respectively three and two decimal points below the expected in 1Q25.
(f): forecast.
Source: BBVA Research

Weaker US growth on higher uncertainty, weaker 1Q25 data (to be partially offset by a 2Q25 rebound); growth will be backed by lower US tariffs and economic stimuli in China, and by defense and infrastructure spending as well as by lower inflation and interest rates in the Eurozone

Inflation is still likely to rebound in the US following tariff hikes, and to remain contained in the Eurozone and China

HEADLINE CPI INFLATION
(Y/Y %, AVERAGE OF THE PERIOD, CHANGE WITH RESPECT TO PREVIOUS FORECAST IN PARENTHESES)

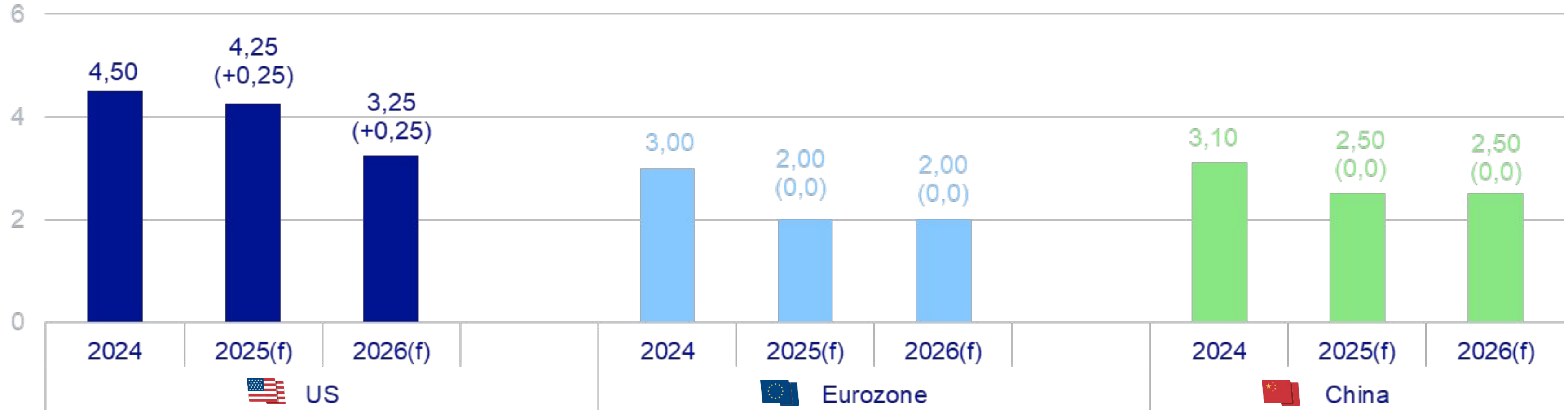


(f): forecast.
Source: BBVA Research

Lower energy prices, weak demand pressures and stronger support controlled inflation, except in the US, where tariffs are likely to raise production costs; a stronger euro is also likely to keep inflationary pressures limited in Europe

The Fed will keep rates unchanged for longer given tariff uncertainty; ECB monetary tightening is likely over

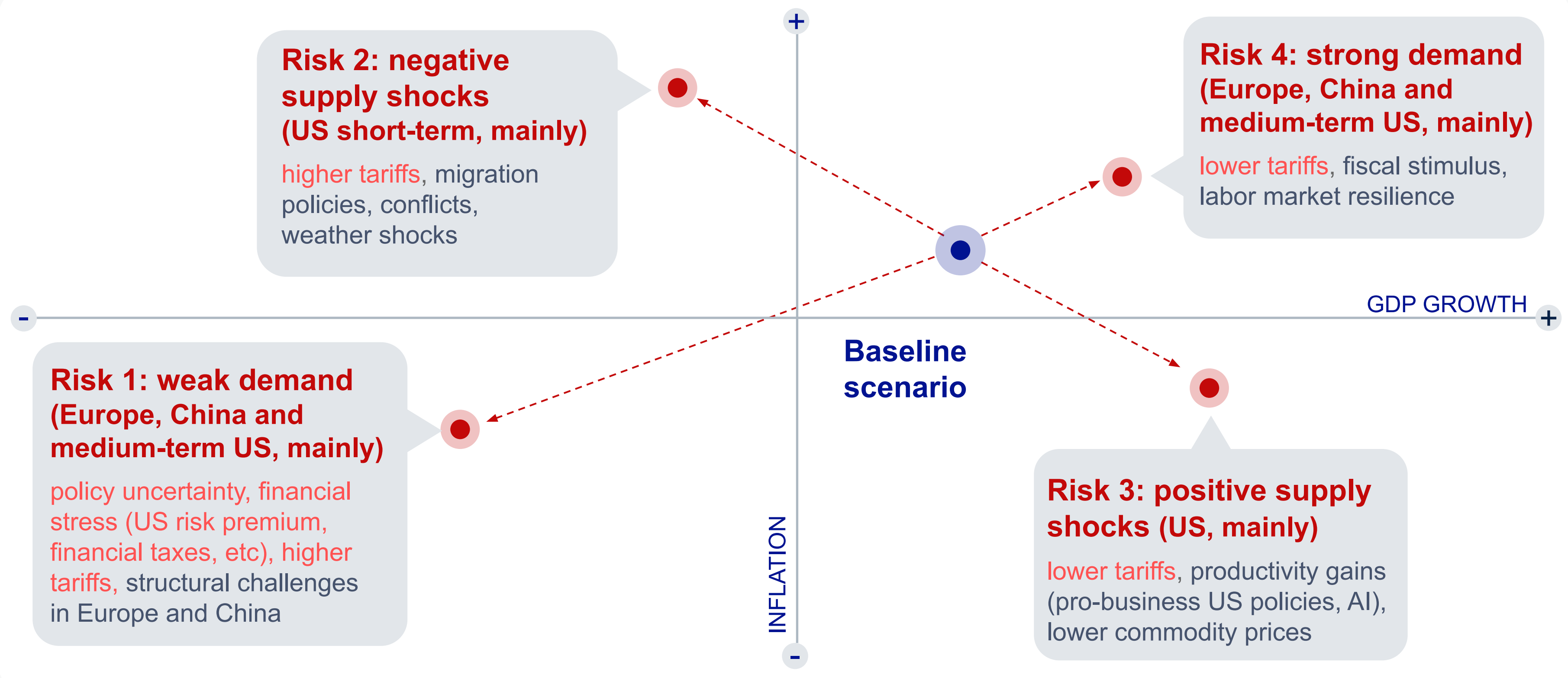
POLICY INTEREST RATES (*)
(%, END OF PERIOD, CHANGE WITH RESPECT TO PREVIOUS FORECAST IN PARENTHESES)



(f): forecast.
(*) In the case of the Eurozone, interest rates of the deposit facility.
Source: BBVA Research.

The Fed is forecast to cut rates once this year (in 4Q25), but the easing cycle would continue in 2026, at least if inflation rebound on tariffs proves to be temporary; in the Eurozone, rates are forecast to remain at 2%, but growth concerns and controlled inflation could pave the way for extra cuts

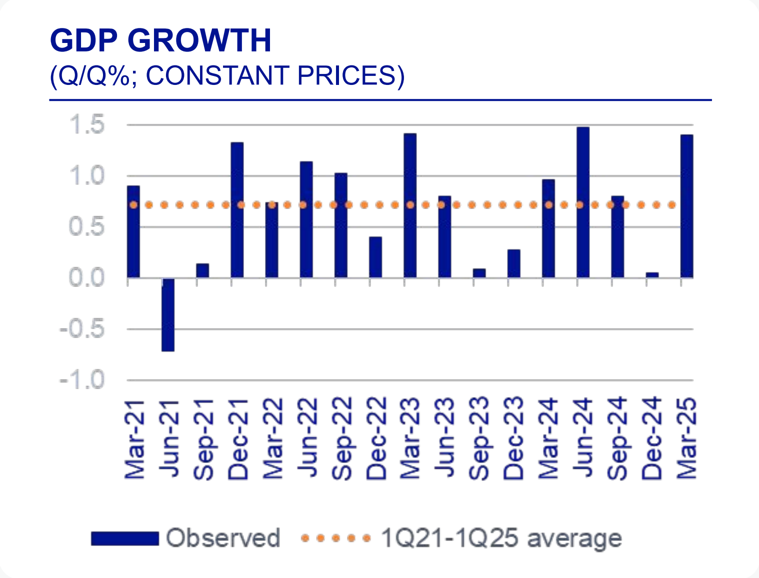
Risks: mainly on greater uncertainty and rising US risk premium; tariff risks are also higher, but more balanced



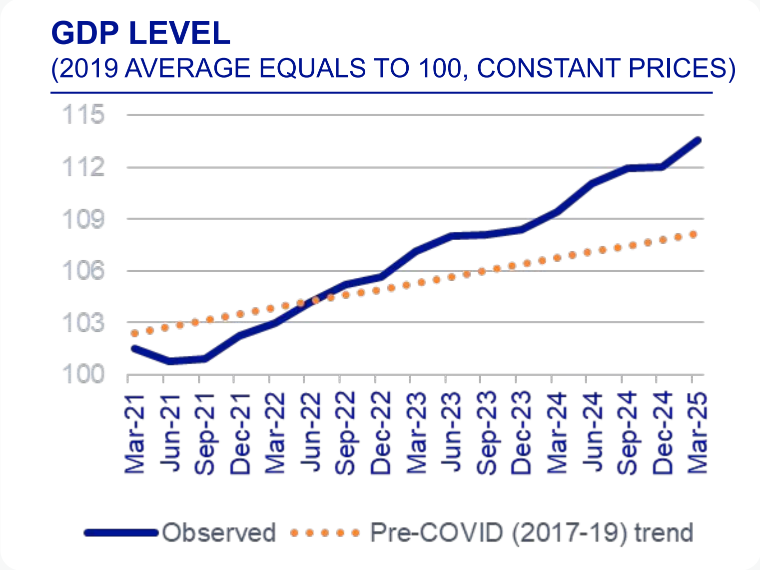
Research

Brazil Outlook

Dynamic economic activity at the beginning of 2025: GDP growth rebounded more than expected in 1Q25



Source: BBVA Research based on data by IBGE.

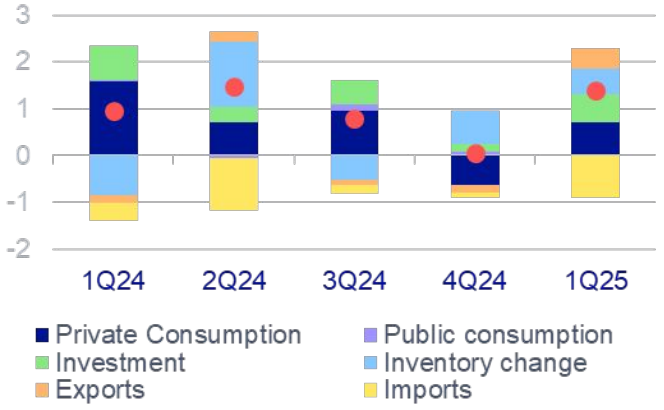


Source: BBVA Research based on data by IBGE.

1Q25 GDP expanded 1.4% q/q , much higher than both our forecast (0.6% q/q) and growth in the previous quarter (0.1% q/q); despite recent growth volatility, GDP remains well above the pre-COVID (2017-19) trend

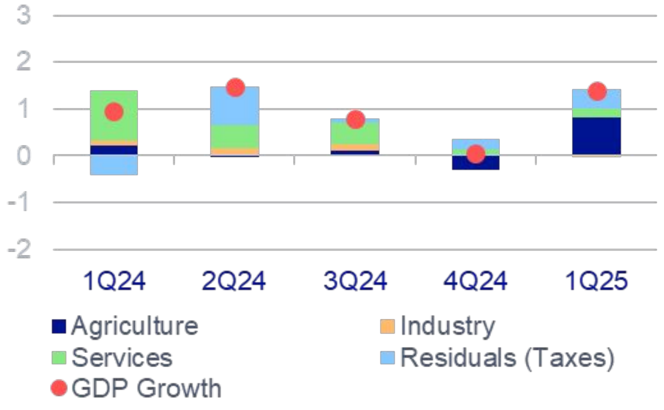
The strong performance of the agriculture sector was the main driver of growth in the 1Q25

CONTRIBUTION OF DEMAND COMPONENTS TO QUARTERLY GDP GROWTH (GDP GROWTH: Q/Q%; CONTRIBUTIONS TO GROWTH: PP)



Source: BBVA Research based on data by IBGE.

CONTRIBUTION OF SUPPLY COMPONENTS TO QUARTERLY GDP GROWTH (GDP GROWTH: Q/Q%; CONTRIBUTIONS TO GROWTH: PP)

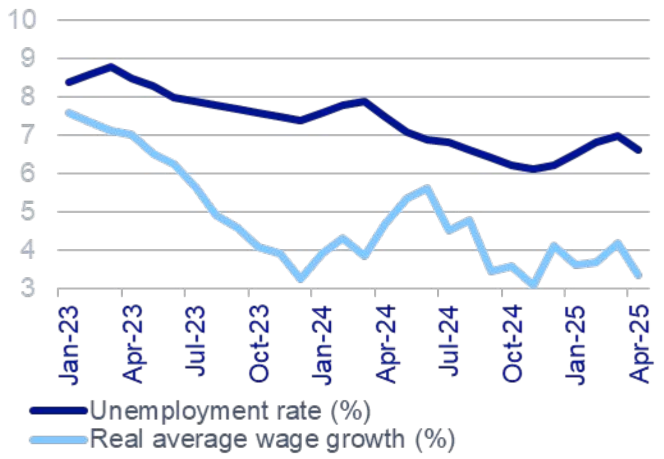


Source: BBVA Research based on data by IBGE.

The agriculture sector grew by 12.2% q/q in 1Q25, driven by a bumper soybean harvest; private consumption recovered from a contraction in 4Q24, while investment accelerated; although exports increased, their contribution to GDP growth was offset by a sharp rise in imports

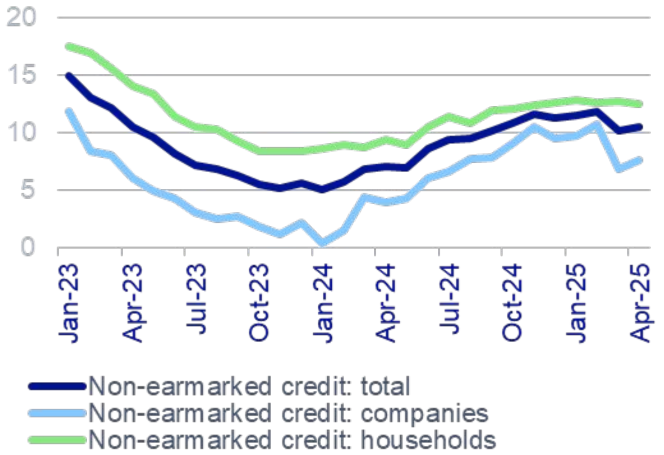
Most recent data suggest that despite incipient deceleration, economic activity remains resilient

UNEMPLOYMENT RATE AND REAL AVERAGE WAGE GROWTH (%)



Source: BBVA Research based on data by the BCB.

CREDIT STOCK: NOW-EARMARKED LOANS (Y/Y %)

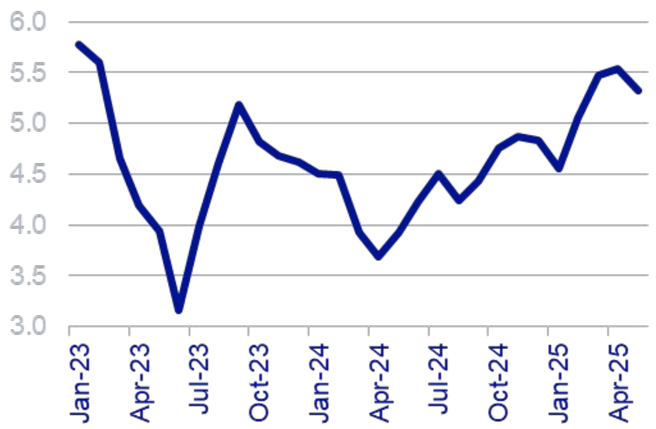


Source: BBVA Research based on data by the BCB.

Labor and credit markets remain relatively solid despite recent signs of weakening: the unemployment rate has edged up, real wage growth has eased, and overall credit growth has slowed since late 2024

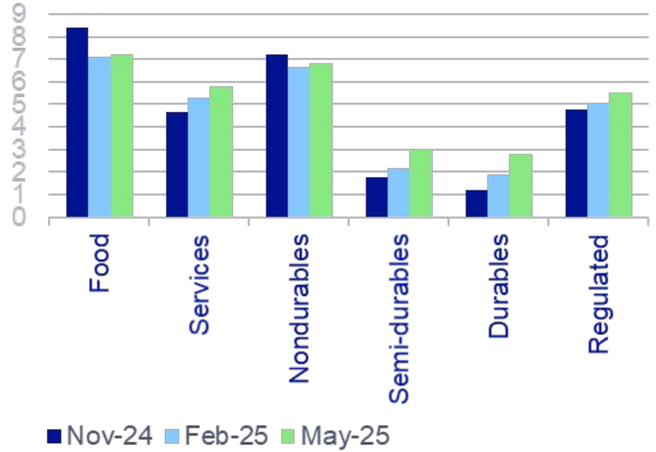
Inflation remains high, above the 1.5%–4.5% target range, but recent signs of moderation have emerged

HEADLINE INFLATION: IPCA
(%)



Source: BBVA Research based on data by the BCB.

INFLATION COMPONENTS: IPCA
(%)

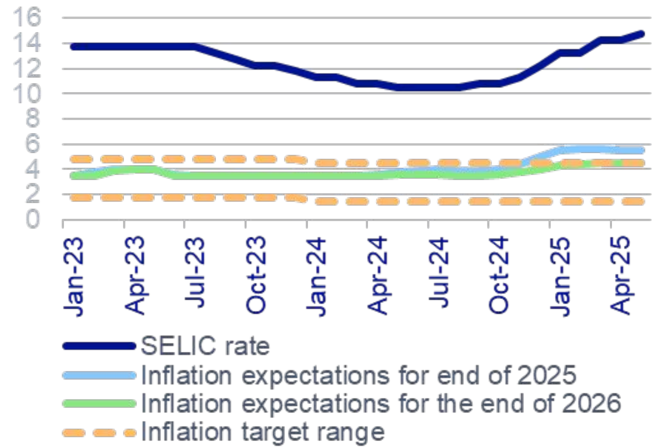


Source: BBVA Research based on data by the BCB.

Inflation continues to be driven by still solid domestic demand, the lagged (and now fading) effects of the exchange rate depreciation in 2024 and some local supply shocks, but has been lower than expected in recent months

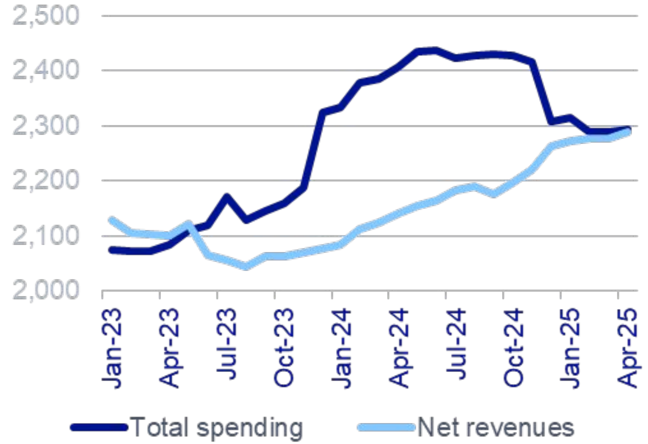
Economic policies have gradually become more restrictive

SELIC INTEREST RATE, INFLATION EXPECTATIONS (%)



Source: BBVA Research based on data by the BCB.

CENTRAL GOVERNMENT PRIMARY RESULTS: ACCUMULATED OVER THE LAST 12 MONTHS (R$ BILLION; CONSTANT PRICES, AS OF APR/25)

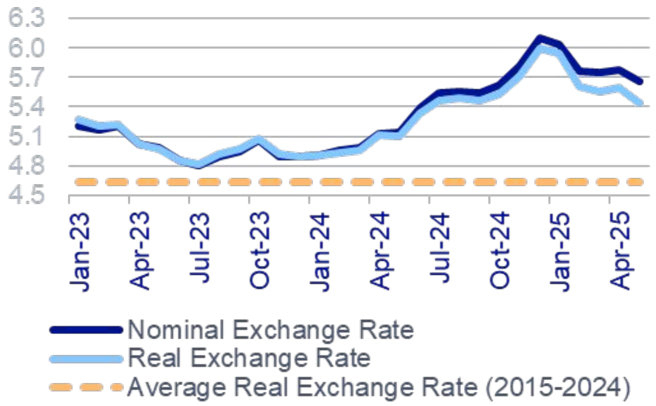


Source: BBVA Research based on data by the BCB.

Monetary conditions are clearly tight as the SELIC rate is now well above its estimated equilibrium level of around 10%; fiscal impulse has declined after having reached very large levels in 2023-24

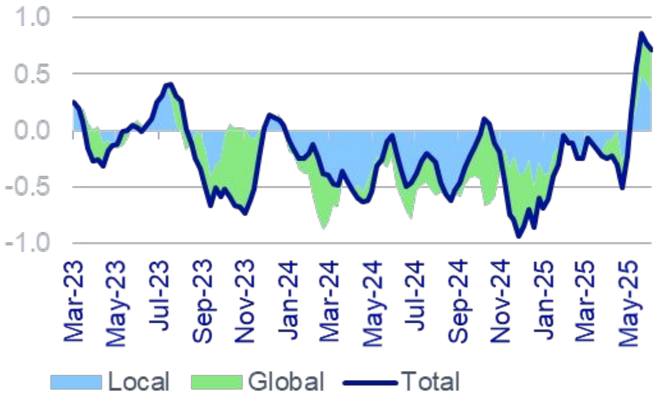
The Brazilian real has continued to appreciate over the last few months, reversing part of the 2024 losses

NOMINAL AND REAL EXCHANGE RATE
(BRAZILIAN REAL PER USD, REAL EXCHANGE RATE AT MAY/25 PRICES)



Source: BBVA Research based on data by the BCB.

PORTFOLIO FLOWS TO BRAZIL: LOCAL AND GLOBAL FACTORS DECOMPOSITION
(4-WEEK MOVING AVERAGE, Z-SCORES)

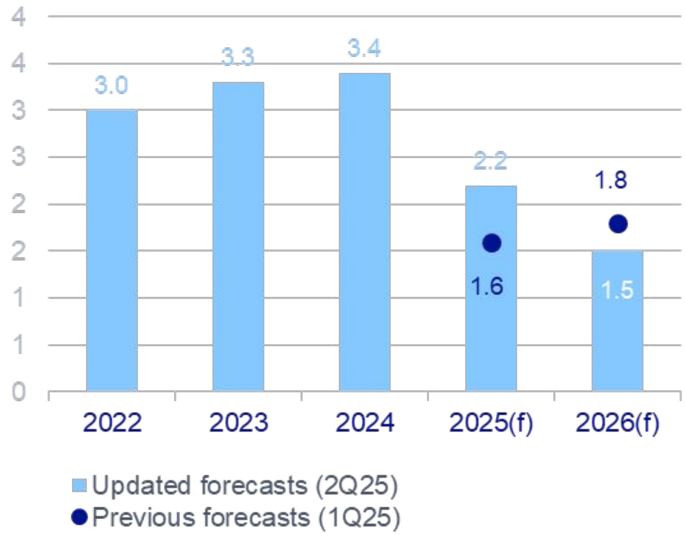


Source: BBVA Research based on data by Haver.

The Brazilian real has appreciated 10% year-to-date, after having lost almost 30% in 2024; the ongoing recovery is related to global factors (mainly the USD weakness) and local issues (such as the sharp increase of the Selic rate)

Growth is likely to ease, but the 2025 forecast has been revised up on strong 1Q25 data, despite the global context

GDP GROWTH
(%)

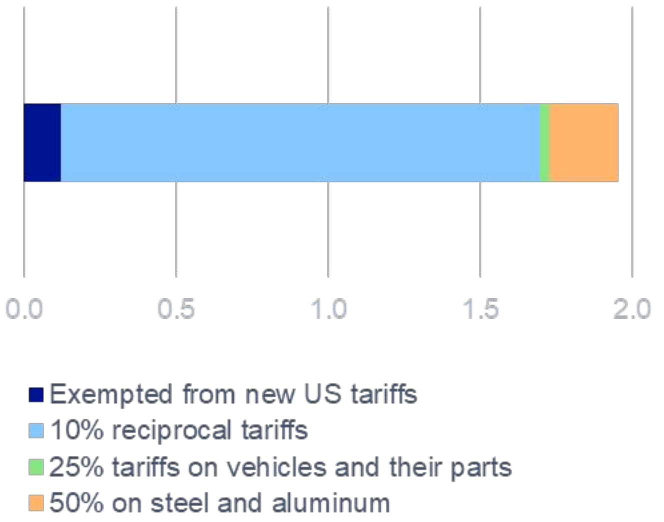


- Higher-than-expected growth in 1Q25, led by the agriculture sector, sets the stage for growth above 2.0% this year
- Still, **a less supportive global environment and tighter domestic policies locally reinforce deceleration prospects**
- Low growth is expected, mainly in the second half of 2025, and to continue into next year
- Growth could exceed forecasts if the primary sector continues to outperform and domestic demand proves more resilient than expected
- But there are also downside risks to growth, mainly due to global factors and domestic fiscal vulnerabilities

(f): forecast.
Source: BBVA Research.

Brazil is not particularly exposed to US policies, but it will also be affected by a more negative global environment

BRAZIL'S EXPORTS TO THE US, BY US TARIFF LEVEL (*) (% OF GDP, 2024)

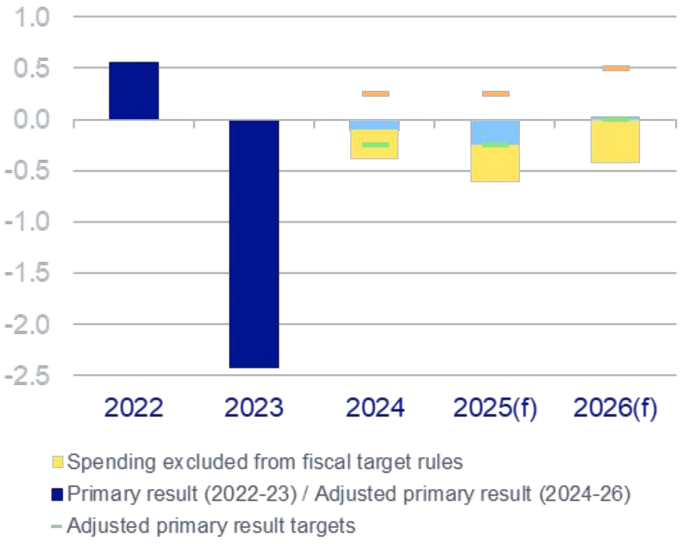


- Brazil's exports to the US represent only around 2% of its GDP
- Most of these exports now face a 10% tariff, while the vehicle industry and, especially, the steel and aluminum sectors face higher tariffs
- **Our calculations suggest the average US tariff on Brazil's exports has increased by around 14pp this year, which could reduce GDP by 0.2 percentage points**, assuming an import demand elasticity of 0.8
- **Although Brazil's direct exposure to US tariffs is limited, the country will also be affected by lower global growth and less favorable terms of trade**, given the prospects of lower commodity prices

(*): US tariff level estimated with information until June 9, 2025. Export figures refer to exports as a share of GDP using 2024 data..
Source: BBVA Research based on data by the US Census Bureau and IBGE.

Fiscal targets will likely be met, but a structural adjustment of fiscal accounts is unlikely, at least in 2025-26

CENTRAL GOVERNMENT PRIMARY RESULT (% OF GDP)

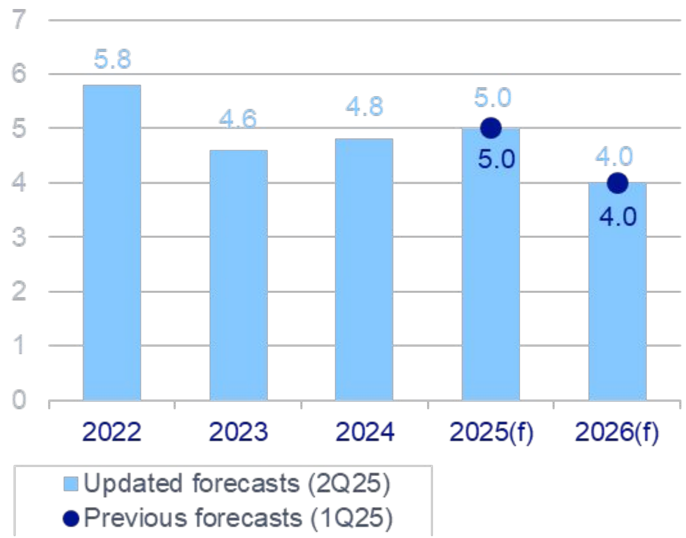


- We continue to expect addiitonal fiscal measures to help the government to reduce the fiscal impulse and meet the adjusted fiscal targets (primary result of 0% of GDP in 2025, 0.25% in 2026, with a ± 0.25pps tolerance range)
- **But contained primary deficits are not enough to prevent further fiscal deterioration**: large interest payments will likely keep the total deficit between 8% and 9% of GDP in 2025-26, and public debt is expected to continue trending upwards, approaching the 85% mark in 2026
- Although we still see a muddle-through scenario—where a fiscal crisis is avoided—as the most likely outcome, there is a risk that policy mismanagement, or other negative shocks, could further worsen fiscal expectations, ltriggering macroeconomic and financial turbulence

(f): forecast.
Source: BBVA Research.

Inflation is expected to ease moving forward

HEADLINE INFLATION: IPCA
(YOY%, END-OF-PERIOD)

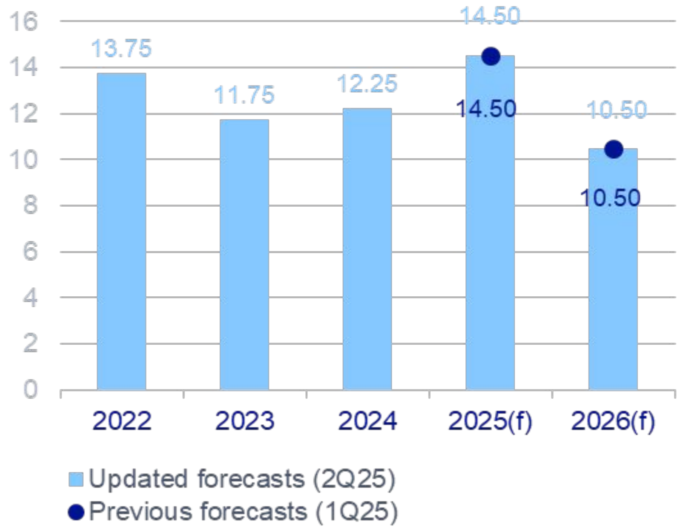


- Inflation is forecast to gradually slow, reflecting both global and local factors
- On the global front, growth will likely lose steam, commodity prices are expected to be lower than previously anticipated and US tariffs could create an abundant supply (from China, for example) that puts downward pressure on global prices
- Moreover, **inflation is set to benefit from a weaker domestic demand and a stronger Brazilian real**
- However, fiscal risks are likely to continue weighing on expectations and labor markets are likely to remain broadly tight, hindering a convergence of inflation to the 3.0% target

(f): forecast.
Source: BBVA Research.

The tightening cycle is mostly over, but the Selic rate will likely stay at restrictive levels for an extended period

SELIC INTEREST RATE
(YOY%, END-OF-PERIOD)

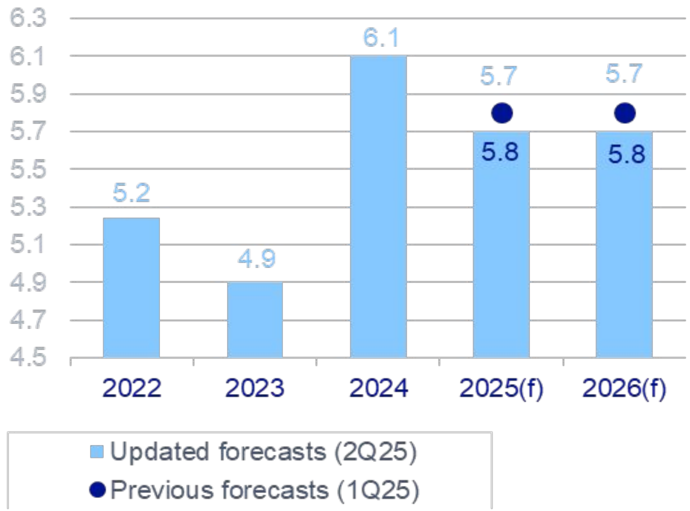


- The Selic rate reached 14.75% in May/25 and a final +25bp hike in Jun/25 is still forecast given resilient domestic demand; however, the central bank could rather take comfort in recent downside surprises in inflation and put and end the tightening cycle
- **An easing cycle could be launched at the end of the year**, when inflation will likely be more controlled, growth will have weakened and the Fed is expected to resume its easing cycle
- Still, **rates are expected to remain at restrictive levels during 2025-26** as inflationary pressures are unlikely to fully subside

(f): forecast.
Source: BBVA Research.

A globally weaker dollar supports a more appreciated exchange rate

NOMINAL EXCHANGE RATE
(BRL / USD, END-OF-PERIOD)



- **We expect the exchange rate to remain around 5.7, but risks are tilted towards lower levels**
- The main driver of a stronger-than-expected Brazilian real is the global weakening of the dollar, reflecting rising concerns over US policies
- In addition, high Selic rates and more controlled fiscal risks also support the Brazilian real
- Volatility is expected ahead of the 2026 general elections

(f): forecast.
Source: BBVA Research.

BBVA Research forecasts for Brazil

		2022	2023	2024	2025 (f)	2026 (f)
GDP (%)	Updated (2Q25)	3.0	3.2	3.4	2.2	1.5
	Previous (1Q25)				1.6	1.8
Inflation (%, end-of-period)	Updated (2Q25)	5.8	4.6	4.8	5.0	4.0
	Previous (1Q25)				5.0	4.0
Policy rate (%, end-of-period)	Updated (2Q25)	13.75	11.75	12.25	14.50	10.50
	Previous (1Q25)				14.50	10.50
Exchange rate (end-of-period)	Updated (2Q25)	5.24	4.90	6.10	5.70	5.70
	Previous (1Q25)				5.80	5.80

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