

# Brazil: An Attractive Entry Point

By Malcolm Dorson, Senior Portfolio Manager



São Paulo, Brazil

We believe the recent global market volatility has created an attractive entry point for Brazilian equities. Asset prices have seen a violent pullback due to market sentiment around recent COVID-19 headlines, but Brazil's investment case continues to improve as the country moves from recovery to growth and, in our view, a compelling turnaround opportunity. After 13 years of subsidy-led wealth redistribution and unfriendly business policies, Brazilians elected a new government in late 2018 under the leadership of President Jair Bolsonaro. The new government cracked down on corruption and showed prudence in its central bank policies. Between President Dilma's 2016 impeachment and December 31, 2019, Brazil's stock index, the Bovespa, surged 60.9%,<sup>1</sup> despite persistently high unemployment and low economic growth. We credit much of the market optimism to the country's significant reform programs and future prospects for growth. Year-to-date, global volatility has driven the Bovespa down 47.7%, and we believe that prices have dislocated from fundamentals.<sup>2</sup>

## An improving backdrop

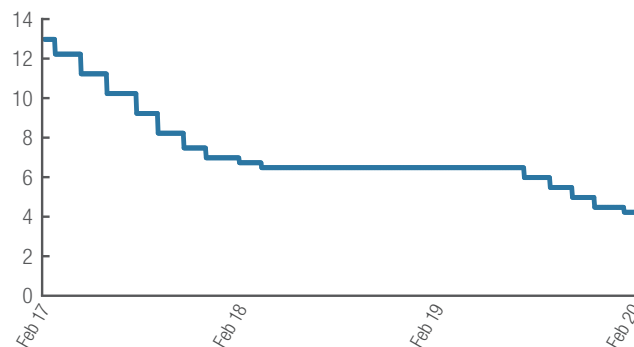
### Policies

Since peaking at 10.2% in 2015, Brazil's fiscal deficit is expected to decline to 4.9% of GDP by 2021. Finance Minister Paulo Guedes has helped Brazil avoid a fiscal cliff via structuring and passing significant social security reform in 2019. The plan is expected to save Brazil roughly BRL800 billion over 10 years, which is well above the market's initial estimates. Furthermore, additional privatization, tax reform, and trade liberalizations should help mitigate macroeconomic shocks in the future, which were once common in Brazil, giving investors greater comfort when investing in the country.

### Interest Rates

With historically low inflation, the central bank saw an opportunity to continue to cut interest rates. As of February 29, 2020, the central bank had cut the Selic rate by 1,000 basis points since November of 2016. Given Brazil's history of hyper-inflation, most companies are levered in floating rate debt, and the dramatic drop in interest rates has translated into a strong wave of lower interest expenses and positive earnings revisions.

#### Brazil Selic Target Rate



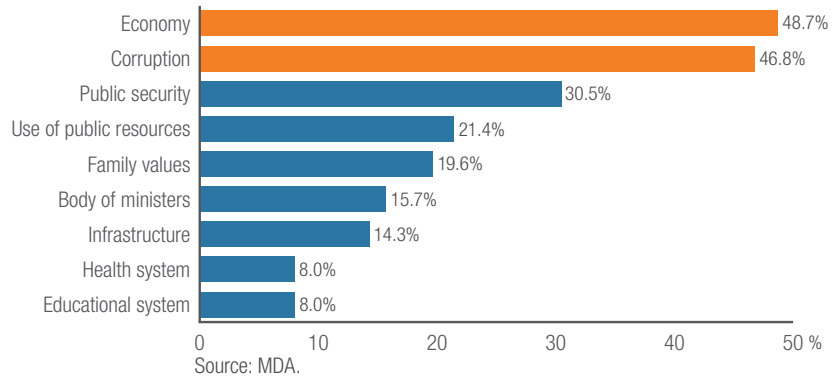
Source: Bloomberg.

# Where are we now?

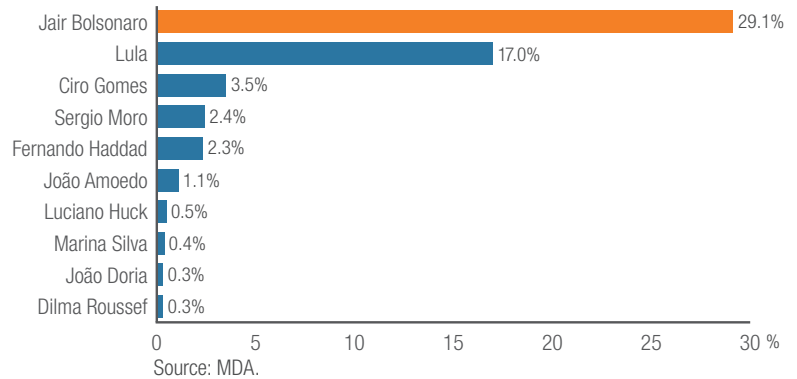
## Political Continuity

With a focus on attacking corruption, reducing bureaucracy, and increasing the pace of privatizations, the market has viewed Bolsonaro as a business friendly president. Though Brazil is approaching mid-term elections at the end of 2020, we believe the market should price in continuity and expansion of pro-market policies. Not only does Bolsonaro hold a strong lead in the polls, but Brazilians are giving him credit for following through on his top election pillars in improving the economy and cracking down on corruption.

### Improvements Under Bolsonaro



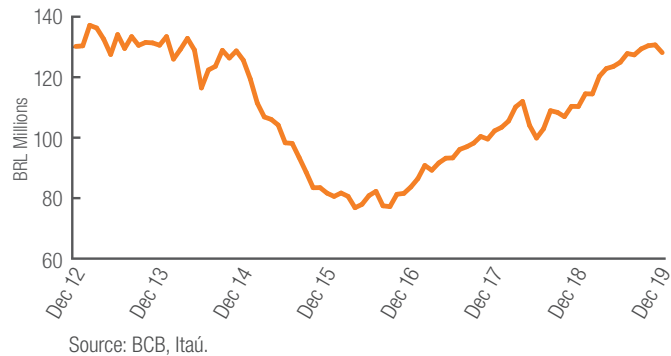
### 2022 Presidential Race Polls



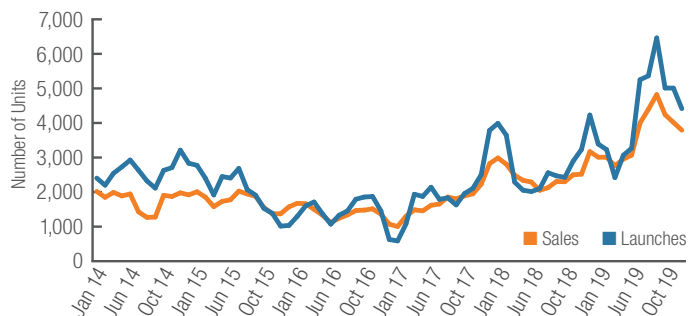
## Economics

Though GDP, by relative standards, remains tepid, the trend is positive and economic indicators appear favorable. Lower interest rates not only reduce corporate financial expenses, but they also spur the economy as seen through new vehicle loans and real estate launches.

### New Vehicle Loans



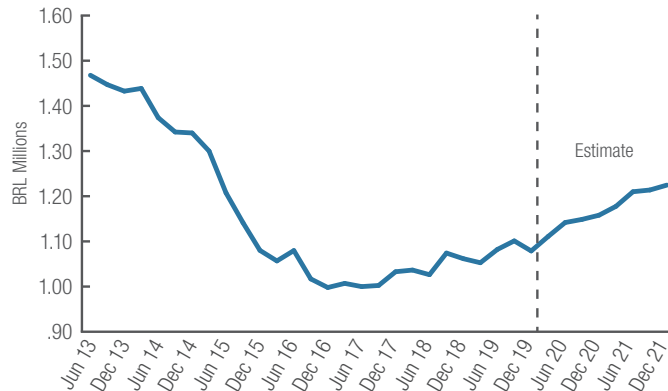
### São Paulo Real Estate



Brazilians and Brazilian corporations are spending more, which creates new jobs and economic growth. After losing over 1 million jobs during the last recession from 2015-17, Brazil has finally turned the corner. The country created 185 thousand formal new jobs in 2019, with the pace of formal job creation accelerating every quarter.

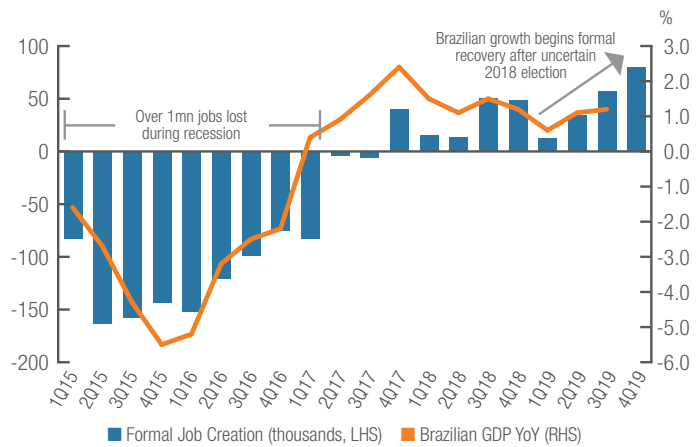
Job creation is also leading to improved credit quality, as banks are seeing fewer late payments and improved delinquency ratios.

### Investments are Expected to Increase



Source: IBGE, Itaú. Estimates are projections and not guarantees.

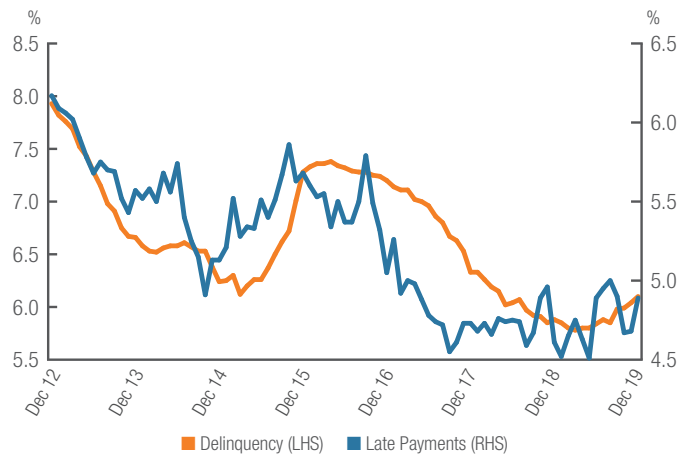
### Consistent New Job Creation



Source: MTE, Itaú. LHS = left hand side, RHS = right hand side.

After 13 years of subsidy-led wealth redistribution and unfriendly business policies, Brazilians elected a new government in late 2018 under the leadership of President Jair Bolsonaro.

### Improvements in Delinquency Rates & Late Payments



Source: BCB, Itaú. Based on Brazilian Households. LHS = left hand side, RHS = right hand side.

## But what about coronavirus?

Though the number of confirmed COVID-19 cases in Brazil remains relatively limited, we have seen significant impacts on global commodity prices, as contagion fears have translated into downgrades for economic activity and demand expectations. With increased contagion, a possible supply chain disruption in Brazil could impact value chains and hurt near term earnings. That said, as long term investors, we believe that the headline driven volatility has also created a window to invest in an improving political and economic backdrop at more attractive valuations.

We believe that Brazil has turned the corner. The combination of lower interest rates, improved economic policies, and a stable political outlook create an attractive back-

drop for investment opportunities across the country. Recent supply increases in Saudi Arabia and Russia have also led to dramatically lower oil prices, providing Brazil with a softer base for comparisons looking forward. We acknowledge that Brazil still faces various obstacles and is far from an investment utopia, but the country is coming from a low base, and in our experience, sometimes the low hanging fruit is the most rewarding. We maintain our preference for companies with strong management teams who also benefit from a backdrop of structural growth. In broad terms, we seek companies presenting above average growth, proven cash generation, that trade below their intrinsic values.

---

The combination of lower interest rates, improved economic policies, and a stable political outlook create an attractive backdrop for investment opportunities across the country.

---

---

### Sources and Important Information

<sup>1</sup>Source: Bloomberg, from August 31, 2016 to December 31, 2019. the Bovespa index is shown in USD terms.

<sup>2</sup>Source: Source: Bloomberg, as of March 12, 2020, the Bovespa index is shown in USD terms.

**Basis Point (bp)** is a unit that is equal to 1/100th of 1% and is used to denote the change in the value or rate of a financial instrument. **Gross Domestic Product (GDP)** is the monetary value of all the finished goods and services produced within a country's borders in a specific time period. **Fiscal Deficit** is a shortfall in the government's income compared with its spending.

*Past performance is no guarantee of future results.*

**Investment Risk** — There can be no guarantee that any investment strategy (risk management or otherwise) will be successful. All investing involves risk, including the potential of loss of principal.

**Emerging Markets Risk** — The risks of foreign investments are typically greater in less developed countries, which are sometimes referred to as emerging markets. For example, legal, political and economic structures in these countries may be changing rapidly, which can cause instability and greater risk of loss. These countries are also more likely to experience higher levels of inflation, deflation or currency devaluation, which could hurt their economies and securities markets. For these and other reasons, investments in emerging markets are often considered speculative. Similarly, investors are also subject to foreign securities risks including, but not limited to, the fact that foreign investments may be subject to different and in some circumstances less stringent regulatory and disclosure standards than US investments.

**An investor should consider the Fund's investment objectives, risks, charges and expenses carefully before investing. This and other important information about the investment company can be found in the Fund's prospectus and summary prospectus. To obtain a prospectus or summary prospectus, please contact your financial advisor or call (888) 335-3417. Please read the prospectus carefully before investing.**

Mirae Asset Global Investments (USA) LLC is the investment advisor for the Mirae Asset Discovery Funds.

---

Mirae Asset Discovery Funds are distributed by Funds Distributor, LLC.

Copyright © 2020 by Mirae Asset Global Investments (USA) LLC. All rights reserved.

Mirae Asset Global Investments (USA) LLC ■ 625 Madison Avenue, 3rd Floor, New York, NY 10022 ■ (888) 335-3417 ■ [investments.miraeasset.us](https://investments.miraeasset.us)

BRTC-SS-0320