

The Local Flavor

Brazil

Sergio Goldman

+55 (11)3089-8747 (2019)
sgoldman@bulltick.com

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Labor market woes continue to deteriorate sentiment

In the last few days, one of the most debated issues in Brazil has been what the Government can and will do to try to minimize the risks of a sharp increase in unemployment.

Yesterday, the Labor Minister reported that over 650,000 formal job positions were eliminated in December, a number twice as big as what was experimented in the previous years.

While such a negative number was already expected, its report seems to have deteriorated further the already sour sentiment.

We would like to include in this piece the table we put in the short Note we published yesterday when December's formal jobs elimination was released.

Exhibit 1. Evolution of Formal Jobs Created/Elimin. in Brazil's Economy After Crisis Intensified

Sector	October 2008	November 2008	December 2008	After-Crisis Jobs Elimination	Full Year 2008
Mineral Extraction	91	(1,182)	(3,121)	(4,212)	8,671
Transformation Industry	8,730	(80,789)	(273,240)	(345,299)	178,675
Public Utilities	(674)	(950)	(980)	(2,604)	7,965
Civil Construction	2,149	(22,731)	(82,432)	(103,014)	197,868
Commerce	54,590	77,886	(15,092)	117,384	382,218
Services	36,142	39,296	(117,128)	(41,690)	648,259
Public Administration	(1,205)	(1,829)	(28,466)	(31,500)	10,316
Agriculture	(38,422)	(50,522)	(134,487)	(223,431)	18,232
Total	61,401	(40,821)	(654,946)	(634,366)	1,452,204

Source: Caged, Bulltick

Investors should have in mind that the sector with the largest number of formal jobs eliminations was the transformation industry, followed by the agriculture sector.

These two sectors were responsible for almost 90% of the job positions closed from October, when the crisis effects started to be felt in a stronger way.

Therefore, any measures to try to limit the number of lay-offs in 1Q09 would have to focus primarily in the industry and agriculture sector.

If implemented as expected, an aggressive reduction in interest rates is expected to help overall sentiment but its impact on the labor market may take a few months to be felt.

Therefore, in order to try to impact almost immediately economic agents' sentiment in the economy as a whole, the Government would have to combine specific sector stimulus with monetary policy.

Funny enough, a lot has been said about the announcement of a series of measures to boost activity in the civil construction sector that would take place by the end of January.

As the table shows, while over 100,000 job positions have been eliminated from the construction sector since October, industry and agriculture seem to be in need of stronger measures.

Brazil's Economic Team may be expecting a migration of job positions from other sectors to the construction sector as the series of measures soon to be announced start to become effective.

What this set of measures to boost activity in the construction sector may include?

1. Increase in the maximum value of properties to be financed with FGTS funds to around R\$500,000 from the current R\$350,000;
2. Deduction from income tax of interest payments on mortgage financing;
3. Reduction of taxes on the civil construction production chain;
4. Institute a bonus for those who do not delay mortgage payments;
5. Create a fund with public funding that will be used as insurance for low income mortgage financing. This measure should impact the population with monthly income of no more than R\$2,000/month and,
6. An increase in Government resources allocated to fund popular housing projects. Part of this increase would be used to create the insurance fund mentioned in the topic above.

Should these measures be actually implemented, they will be positive for Brazil's real estate related stocks, not only for the short term but also for the long term investment case. Actually the sector has been outperforming the market year-to-date on expectations over the announcement of such measures.

We continue to highlight three stocks in the sector at this moment: Cyrela (CYRE3), PDG (PDGR3) and MRV (MRVE3).

Contacts

Brazil:

Sergio Goldman	+ 5511 3089-8747	sgoldman@bulltick.com	Head of Research
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Mexico:

Raul Morales, CFA	+ 52 55 5246-7020	rmorales@bulltick.com	Head of Research Sales
Rodrigo Sotomayor	+ 52 55 5246-7020	rsotomayor@bulltick.com	Sales & Trading
José Arturo Tobias	+ 52 55 5246-7040	jatobias@bulltick.com	Research Analyst

USA:

Alexander Kazan	+ 1 212 616-2603	akazan@bulltick.com	Head of Research Sales
Frederico Fumeni	+ 1 212 616-2604	ffumeni@bulltick.com	Sales & Trading
Mauro Pierre	+ 1 212 616-2604	mpierre@bulltick.com	Sales & Trading

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