Markets are jittery about Brazil's economic fundamentals.

THE YEAR BEGAN with a new round of concerns about emerging countries. As occurred in mid-2013, the group of countries an investment bank has nicknamed "the fragile five"—Brazil, India, Turkey, Indonesia, and South Africa (BITIS)—was particularly penalized.

In its monetary policy report of February 11 the U.S. Federal Reserve Bank (Fed) lists the same five countries as those most vulnerable to changes in U.S. monetary policy, having selected them because among emerging countries they have recorded the largest currency devaluations and the highest rises in interest on their bonds.

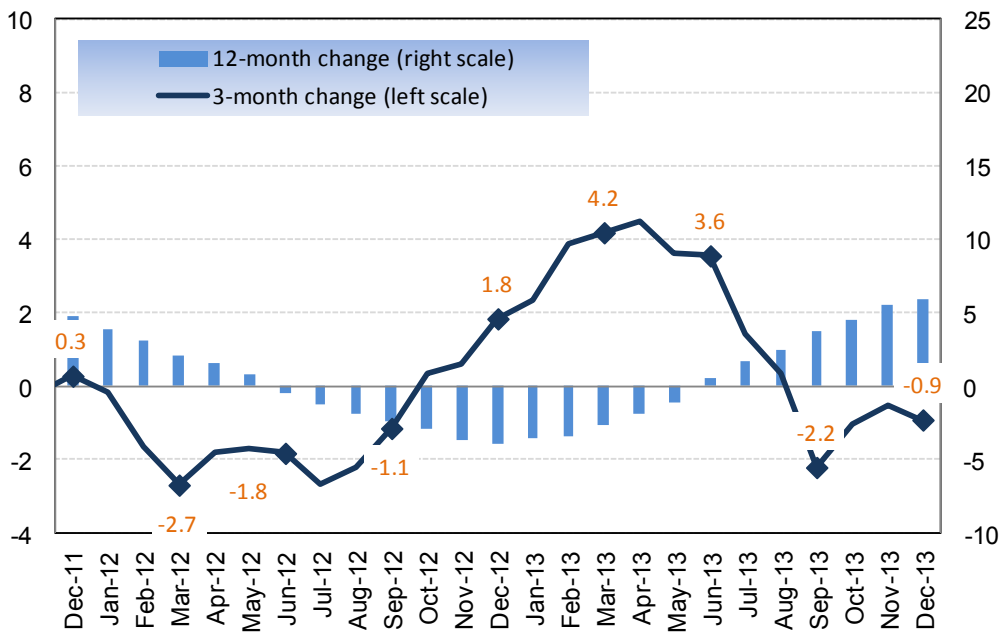
One view is that the BITIS were affected because they have more developed and liquid domestic financial sectors, which allows investors to buy or sell large quantities of their assets at any time at a low transaction cost and buy foreign currency. Another view is that the BITIS have suffered more than other countries because they have weaker economic fundamentals. According to the Fed's vulnerability index, among 15 emerging countries, the only one more vulnerable than Brazil is Turkey.

The change for the worse in market views of Brazil could significantly affect external financing inflows and consequently the real economy. In the second half of 2013, market jitters about Brazil's economic fundamentals helped to slow fixed investment significantly, as the IBRE Monthly Fixed Investment Indicator (IMI) shows.

Our assessment of the Brazilian economy has not changed substantially from previous issues. We estimate that in the fourth quarter of 2013 GDP grew only 0.3% quarter-on-quarter, and only 2.1% for the whole of 2013. Although we hold to our forecast of 1.8% in 2014, we realize that the downside risks to the Brazilian economy are very high, and the pervasive uncertainty that marked the economy in 2013 is likely to continue throughout 2014.

IBRE´s Fixed Investment Indicator is going nowhere.

(Percent change over the previous quarter and 12-month moving average, seasonally adjusted)



Sources: IBGE, Funcex, and IBRE staff.