

Outlook for 2026

Highlights

In this Special Report, we present our expectations for the macroeconomic outlook in 2026. Overall, we assess that the environment should become somewhat more constructive, although the domestic electoral cycle introduces a high degree of uncertainty. In our baseline scenario, we project the exchange rate at BRL 5.50/USD, continued disinflation, further deceleration in economic activity, and the beginning of a monetary easing cycle. In the external environment, we expect the Fed to continue cutting rates, amid moderate growth in U.S. GDP, while inflation still reflects one-off tariff pass-throughs and a gradual slowdown in services inflation.

United States

Trade Policy

The first year of Trump's second term was marked by an intensification of the trade war. Initially, tariffs were imposed on China, Mexico, and Canada, alongside sectoral tariffs on vehicles, auto parts, steel, aluminum, and other products. In April, the so-called Liberation Day brought higher tariffs, followed by a broader commercial escalation. Tariffs were subsequently reduced through July, when Trump signed letters setting new tariff rates for several countries – particularly higher for Southeast Asian economies accused of triangulating Chinese products. Brazil was also targeted, facing higher tariffs without a clear commercial rationale, in a move with a strong political bias; negotiations remain ongoing.

On the agreements front, the first trade deal was signed with the United Kingdom in May, followed by Japan and the European Union in subsequent months. As a result, effective import tariffs rose to around 17%, generating close to USD 200 billion in import tax revenue in the fiscal year ending in September.

Trump's authority to impose reciprocal tariffs under the International Emergency Economic Powers Act (IEEPA) is being challenged at the Supreme Court, with a ruling expected in late 2025 or early 2026. If overturned, questions remain about tariff refunds and the impact on fiscal revenues. Even so, Trump could still resort to Section 301 (lengthy investigations), Section 122 (a 15% tariff for up to 150 days), or Section 338 of the 1930 Trade Act, which allows retaliation against discriminatory practices with tariffs of up to 50% without extensive investigations.

Fiscal Policy

On the fiscal front, the key development was the approval of the so-called One Big Beautiful Bill, considered the largest tax and budget reform ever passed in a single package. The estimated impact is around USD 3.4 trillion added to public debt over the next decade, significantly widening the structural deficit. The law consolidated core elements of Trump's agenda, including the extension of the TCJA, cuts to corporate and personal income taxes, exemptions on tips and payroll contributions, among other measures. It also partially rolled back green subsidies, redirecting resources toward traditional energy sectors, in line with a pro-fossil fuel stance.

Despite initial popularity, the package has drawn attention to the sharp increase in debt over the next ten years. The combination of tax cuts and the absence of offsetting measures reinforced the perception that the administration is willing to tolerate larger deficits as a political strategy. In parallel, DOGE implemented selective spending cuts, including layoffs in the civil service and restrictions on social programs, contributing to the stalemate that led to a 43-day government shutdown. The 2025 fiscal outcome showed deterioration, with a wider deficit and an accelerating debt trajectory, and pressures are expected to persist into 2026.

Economic Activity

Trade policy dynamics strongly influenced activity in the first half of the year. Through March, imports surged as firms attempted to front-run higher tariffs, boosting first-quarter GDP, while consumption slowed amid uncertainty. In the second quarter – marked by Liberation Day and a 90-day trade truce – the pattern reversed: imports fell and private consumption rebounded. Federal government consumption, however, detracted from growth due to DOGE-led spending cuts, including public-sector layoffs.

More recently, consumption has been increasingly supported by higher-income households, benefiting from rising financial and real estate asset prices, while lower-income groups have adjusted spending in response to declining purchasing power. This contrast has reinforced a “K-shaped” recovery, with wealthier segments expanding consumption and investment, while lower-income households face mounting constraints. In addition, announcements of new investments in data centers and AI-related projects have gained prominence, suggesting that U.S. growth in 2026 may be increasingly driven by advanced technology sectors, even amid heightened trade and fiscal uncertainty.

Labor Market

After resilience at the end of 2024, the labor market slowed throughout the first half of 2025. In July, significant downward revisions to May and June payrolls raised concerns about labor market health. The unemployment rate remained relatively stable due to reduced labor supply, stemming from Trump’s immigration policy and deportations that lowered labor force participation. More recently, a rise in participation has pushed unemployment higher.

Inflation

At the start of the year, stronger tariff impacts on imported goods prices were expected, with persistent effects on basic inputs. Inventory buildup during the trade truce and, more recently, moderate price pass-through by retailers – concerned about losing market share – have limited immediate inflationary effects. Larger pass-throughs are still expected as margins compress, but the Fed views the impact as largely transitory.

Services inflation remains elevated, above 3%, but shows signs of deceleration in categories such as housing, contributing to a gradual downward trajectory. In a midterm election year, Trump has been particularly sensitive to inflation, the issue with the highest voter disapproval. Despite denying tariff effects, recent price increases in items such as meat and coffee have led the president to negotiate tariffs with Brazil, a key supplier.

Monetary Policy

The Fed held the policy rate at 4.5% for most of the year, amid uncertainty surrounding Trump's policies, particularly on trade. Communications emphasized caution, awaiting the effects of tariffs on inflation, labor markets, and activity. Downward revisions to payroll data in July and rising unemployment from September onward shifted the outlook, culminating in three consecutive rate cuts in the final meetings of the year.

For 2026, the latest statement signaled a pause, reinforced by Chair Powell's assessment that monetary policy is well positioned. Nonetheless, uncertainty remains given the end of his term in May. Trump harshly criticized the rate stance, attempted to remove Powell for non-monetary reasons, and unsuccessfully sought to oust Governor Lisa Cook, in efforts to influence the Board and regional Fed leadership.

Stephen Miran, then chair of the Council of Economic Advisers, was nominated to fill Kugler's seat. Attention now turns to Powell's successor, with polls pointing to Kevin Hassett – a close Trump ally – who may adopt a more political stance and face the challenge of building consensus around further easing.

For 2026, our baseline assumes a terminal Fed Funds rate of 3.0%, reflecting three additional cuts over the year, contingent on Hassett assuming the Fed presidency. GDP growth is projected at 2.0%, above the 1.7% expected for 2025, supported by expansionary fiscal policy and a less restrictive monetary stance. PCE inflation is projected at 2.7%, still influenced by one-off tariff pass-throughs, while a gradual slowdown in services inflation contributes to convergence toward target. The unemployment rate is expected to return to around 4.4%, supported by improved activity and a recovery in labor force participation, previously constrained by immigration policy.

Brazil

Economic Activity and Labor Market

In Brazil, economic activity slowed in 2025 following the strong expansion of the previous year. Throughout the year, the lagged effects of restrictive monetary policy became more evident, particularly in cyclical sectors. At the end of 2024, market expectations pointed to GDP growth between 1.5% and 2.0% in 2025. While current projections are closer to 2.3%, part of that narrative has materialized, with greater moderation but no sharp slowdown. On the supply side, agriculture met expectations with a record grain harvest and high levels of cattle slaughter, becoming the main growth driver. Other sectors slowed more markedly, particularly manufacturing, while extractive industries offset this with higher-than-expected oil output. In services, after strong growth in 2024, activity decelerated as desired by the Central Bank, showing modest and broadly based growth. On the demand side, gross fixed capital formation and imports stood out, though imports of oil platforms were significant one-off, high-value events. Other components – especially household consumption – showed more pronounced cooling, with forward-looking prospects pointing to continued deceleration.

The labor market remained very tight in 2025, with record employment levels across metrics and the lowest unemployment rate in the historical series, both formal and informal. At the end of 2024, the Focus survey anticipated greater labor market cooling, with unemployment approaching 7% by year-end. Instead, only incipient signs of moderation emerged late in the year, still modest and without signaling a sharp rise in unemployment.

For 2026, we expect continued moderation, with GDP slowing to 1.8%. This scenario incorporates lagged monetary tightening and reduced fiscal impulse, partially offset by income tax reform, particularly supporting household consumption. Agricultural growth should also ease due to smaller grain harvests and lower cattle slaughter, below 2025's record. In the labor market, we expect cooling to materialize gradually, with unemployment rising toward 6%.

Fiscal and Politics

Brazil's fiscal landscape in 2025 was characterized by strong revenue performance alongside persistent spending pressures. Federal revenues are expected to reach BRL 2.896 trillion, according to Prisma Fiscal projections, supported by resilient activity and extraordinary revenue measures. With total central government spending estimated at BRL 2.398 trillion, the primary deficit is projected at BRL 68.2 billion, around 0.53% of GDP – outside the zero-deficit target with a 0.25% tolerance, absent permitted exceptions. Fiscal execution showed two phases: a weaker first half due to delayed budget approval, followed by acceleration in the second half as execution normalized and pent-up payments resumed. Structural rigidity nonetheless deepened, with mandatory spending crowding out discretionary outlays and limiting investment space. Gross public debt is projected at 79.5% of GDP under the Prisma definition, and 91.4% under the IMF's broader metric including central bank holdings.

In 2026, an election year with voting on October 4, the debate is likely to shift toward re-anchoring fiscal policy amid perceptions that the current framework is exhausted. The drafting of the 2027 budget bill is expected to become a key milestone for discussions on a new fiscal rule. This occurs amid weakened budget governance, with Congress – particularly the Lower House – gaining influence over spending execution. Rules mandating that 65% of mandatory amendments be paid by July exemplify the reduced flexibility of the Executive. Any redesign of the fiscal anchor will need to contend with slowing activity and still-restrictive interest rates, raising political costs and complicating the balance between credible consolidation and a debt trajectory that, under the broader metric, approaches 100% of GDP by the end of the decade.

External Accounts

The current account deficit widened again in 2025, mainly reflecting stronger goods imports in line with still-resilient domestic demand and greater penetration of cheaper Chinese products amid global trade redirection. To a lesser extent, higher net outflows of profits and dividends also weighed, while export growth was insufficient to offset these pressures. Bilaterally, exports to the U.S. declined following higher tariffs, but trade redirection and the subsequent removal of tariffs on Brazilian agricultural products mitigated the impact. On the financial account, net FDI inflows strengthened over the year and, on a 12-month basis, slightly exceeded the current account deficit, driven mainly by equity participation and reinvested earnings.

The BRL's appreciation in 2025 was largely driven by a weaker dollar and carry trade gains, which outweighed structural external vulnerabilities. The high interest rate differential, reduced FX volatility, and Brazil's decoupled monetary cycle enhanced the currency's risk-adjusted appeal. Toward December, however, the exchange rate weakened, reflecting primarily election-related noise rather than the usual year-end seasonal deterioration in FX flows – underscoring the political nature of the move.

For 2026, we expect the exchange rate to hover around BRL 5.50/USD, albeit with high volatility tied to electoral uncertainty and the presidential transition. We project a current account deficit of USD 75 billion (3.4% of GDP), reflecting a less favorable trade balance and sizable services and primary income deficits amid elevated profit and dividend remittances. External financing should remain relatively comfortable, with FDI inflows of around USD 75 billion covering most of the deficit.

Inflation

In 2025, inflation followed a gradual disinflation path but remained above the 3% target. Twelve-month IPCA fell from above 5% midyear to 4.46% in November, with core measures converging lower but still elevated. Disinflation was driven mainly by food and industrial goods, supported by BRL appreciation and lower commodity prices in local currency. Services inflation remained high, reflecting inertia, a tight labor market, and a positive output gap. Administered prices also added volatility, particularly through electricity adjustments.

Inflation expectations eased but remained unanchored. Focus survey revisions were concentrated at shorter horizons, while longer-term expectations adjusted only modestly, remaining above target – reinforcing the need for caution in monetary policy.

For 2026, we project IPCA at 4.0%, continuing the disinflation trend. The slowdown should remain concentrated in food and industrial goods, supported by better supply conditions, lower FX pass-through, and softer demand. Services inflation should moderate as the labor market cools, though the pace is uncertain and likely to remain elevated. Key risks include FX volatility during the election cycle and potentially stronger inflationary effects from income tax exemptions via higher disposable income and increased pressure on labor-intensive services.

Monetary Policy

Monetary policy in 2025 was marked by a clearly restrictive stance, with the Copom raising the Selic rate to 15.00% in June and then pausing. The decision reflected the assessment that unanchored expectations, elevated projections, resilient activity, and persistent labor market pressures required a significantly contractionary stance for an extended period. The pause aimed to assess the cumulative effects of tightening, not yet fully visible.

Subsequent meetings reiterated the strategy of holding rates high for longer, emphasizing caution amid elevated uncertainty and flexibility to adjust as conditions evolved – including resuming hikes if necessary. In December, the Central Bank reaffirmed that the current stance is consistent with inflation converging toward target over the relevant horizon, while preserving a cautious bias.

For 2026, we expect the Central Bank to begin easing only in March, consistent with the still-hawkish tone and inflation projections above target at the relevant horizon. The strategy remains anchored in maintaining a significantly contractionary stance for a prolonged period to ensure convergence. We project a gradual easing cycle, with 50 bp cuts per meeting, bringing the Selic rate to 12.25% by year-end.

Macroeconomic projections

	2019	2020	2021	2022	2023	2024	2025	2026
Brazil GDP (%)	1,2	-3,3	4,8	3,0	2,9	3,4	2,1	1,8
Unemployment Rate (average, %)	12,0	13,8	13,2	9,3	8,0	6,6	6,1	6,4
IPCA (Consumer Price Index) (%)	4,3	4,5	10,1	5,8	4,6	4,8	4,4	4,0
Selic Rate (end of period, %)	4,50	2,00	9,25	13,75	11,75	12,25	15,00	12,25
Exchange Rate (end of period, R\$/US\$)	4,03	5,20	5,58	5,22	4,84	6,19	5,50	5,50
Current Account Transactions (US\$ billion)	-68,0	-28,2	-46,4	-53,6	-28,6	-56,0	-76,3	-74,9
Current Account Transactions (% of GDP)	-3,6	-1,7	-2,9	-2,8	-1,4	-2,6	-3,5	-3,3
Trade Balance - BCB (US\$ billion)	26,5	32,4	36,4	44,2	80,5	66,2	52,6	53,6
Foreign Direct Investment (US\$ billion)	69,2	37,8	46,4	87,2	62,0	71,1	66,8	75,0
Foreign Direct Investment (% of GDP)	3,7	2,6	2,8	4,5	2,8	3,2	3,1	3,3
Primary Result of the Central Government (% of GDP)	-1,3	-9,8	-0,4	0,5	-2,3	-0,4	-0,5	-0,5
Gross Public Debt (% of GDP)	74,4	86,9	77,3	71,7	74,3	76,1	79,4	83,7
United States - GDP (%)	2,5	-2,2	6,1	2,5	2,9	2,8	1,7	2,0
United States - PCE (%)	1,4	1,1	4,1	6,6	3,8	2,5	3,5	2,8
United States - Fed Funds Rate (end of period, %)	1,8	0,3	0,3	4,0	5,5	4,5	3,75	3,00

Our team

Andrea Bastos Damico
Chief Economist and CEO
andrea@buysidebrazil.com

Rafaela de Sousa
Economist
rafaela@buysidebrazil.com

Marcelo Alonso
Economist
marcelo@buysidebrazil.com

Mirella Hirakawa
Research Coordinator and
Partner
mirella@buysidebrazil.com

Rita Milani
Economist
rita@buysidebrazil.com

Henrique Miareli
Economist
henrique@buysidebrazil.com

