

Our View On-The-Ground

REGIONAL MARKET VIEWS

Brazil's Election

Fiscal Credibility and the Repricing of Political Risk

Brazil approaches the October 4 presidential election with a combination of political uncertainty, elevated interest rates, persistent fiscal pressures, and an economy that continues to show important sources of resilience. The election will determine not only the presidency, but also governors, senators and members of Congress, making the composition of the next political cycle particularly relevant for the implementation of fiscal and structural reforms.

From a market perspective, however, the central question extends beyond the electoral outcome itself. Brazil's main challenge is increasingly fiscal. Gross government debt reached 82.5% of GDP in July, while the public sector nominal deficit accumulated over twelve months stood at 9.34% of GDP. Interest expenditures alone represented 8.67% of GDP over the same period. These figures illustrate the sensitivity of Brazil's debt dynamics to the combination of high interest rates, primary fiscal performance and economic growth.

This makes the election particularly relevant for financial markets. The next administration will inherit an economy with significant productive capacity, a large domestic market, strong exposure to commodities and a deep financial system, but it will also face the challenge of establishing a credible trajectory for public debt. The market implications of the election are therefore likely to depend less on political rhetoric and more on whether the next government can translate its fiscal strategy into an executable framework capable of stabilizing debt, anchoring inflation expectations and reducing the country's structural risk premium.

- **Luiz Inácio Lula da Silva**

From a fiscal perspective, President Lula's program proposes maintaining the existing fiscal framework. The strategy combines control over the growth of primary expenditures with improvements in the efficiency and quality of public spending, changes in taxation and measures aimed at reducing distortions and tax privileges. Fiscal consolidation is therefore embedded within a broader development strategy rather than being presented primarily as an expenditure-reduction program.

The economic program also places significant emphasis on investment. Infrastructure, industrial development, technological transformation and productive credit are presented as mechanisms to increase productivity and expand Brazil's potential growth rate.

For financial markets, the principal variable under a continuity scenario would be the credibility of the existing fiscal framework. Investors would likely focus on whether expenditure growth remains compatible with the fiscal targets and whether improvements in revenues and economic activity can prevent public debt from continuing to rise faster than nominal GDP.

- **Flávio Bolsonaro**

Flávio Bolsonaro's program proposes a different approach to fiscal policy and the role of the state. Its economic framework emphasizes fiscal consolidation, administrative reform, regulatory simplification, lower taxation, greater private-sector participation and changes to the current fiscal rules.

The proposal explicitly identifies stabilization and subsequent reduction of the debt-to-GDP ratio as a central objective. It proposes achieving persistent primary surpluses, limiting subsidized credit financed by the Treasury, imposing greater control over discretionary spending and strengthening the evaluation of public expenditures. The program also proposes reforms aimed at reducing the size and administrative cost of the federal government, together with a broader privatization agenda and measures intended to increase private investment.

From a market perspective, this framework would shift attention toward implementation. A fiscal rule explicitly oriented toward debt stabilization could alter expectations for long-term public finances, but its effectiveness would depend on the magnitude and timing of expenditure adjustments, the interaction between tax reductions and fiscal revenues, and the capacity of the Executive to obtain congressional approval for structural reforms.

| Fiscal Policy Is the Central Market Variable

Brazil's fiscal position explains why this election has potentially important implications for multiple asset classes.

Gross government debt reached 82.5% of GDP in July, rising 3.9 percentage points from the beginning of the year. At the same time, the twelve-month nominal fiscal deficit reached 9.34% of

GDP. The primary deficit is substantially smaller, meaning that a significant part of the nominal imbalance reflects the cost of servicing the existing stock of public debt. Breaking this cycle requires some combination of stronger primary balances, lower real interest rates, faster economic growth and credible fiscal institutions.

Consequently, the most important post-election signal may not be the initial market reaction to the result, but the fiscal strategy presented by the incoming administration and its ability to establish a credible medium-term trajectory for public debt.

| Monetary Policy and the Cost of Capital

Brazil enters the election with monetary policy still restrictive. The central bank reduced the policy rate in September, while maintaining a cautious assessment of the inflation outlook.

Inflation has moderated, with consumer prices increasing 4.22% over the twelve months through August. However, the central bank's reference scenario still projects inflation above the target over part of the relevant monetary policy horizon, reinforcing the need for restrictive monetary conditions.

Conversely, persistent uncertainty regarding debt stabilization could maintain upward pressure on longer-term yields even as the central bank gradually reduces the short-term policy rate. In that scenario, monetary easing would provide less relief to the broader economy because the sovereign risk premium would continue to keep the cost of capital elevated.

For this reason, the post-election behavior of the yield curve may provide one of the clearest signals of how investors interpret the credibility of the incoming fiscal strategy.

| The Brazilian Real

Brazil's relatively high interest rates can provide support to the real by maintaining an attractive interest-rate differential. At the same time, the currency remains sensitive to fiscal expectations, global risk appetite, commodity prices and international monetary conditions.

A credible improvement in expected debt dynamics could therefore operate through two channels: supporting the currency directly through a lower sovereign risk premium and indirectly by allowing monetary policy to normalize without generating equivalent pressure on inflation expectations.

The opposite mechanism is also possible. A deterioration in fiscal expectations could increase exchange-rate volatility and generate additional inflationary pressure through imported prices, potentially limiting the central bank's ability to reduce interest rates.

This relationship makes the currency an important indicator of whether electoral uncertainty is developing into broader macroeconomic risk or remaining contained primarily within political pricing.

| Brazilian Equities

Higher sovereign yields increase the cost of equity, raise financing costs and reduce the present value of future cash flows. Conversely, a reduction in Brazil's structural risk premium could support equity valuations even without an immediate acceleration in earnings growth. Lower long-term rates would improve financial conditions and potentially increase the attractiveness of domestic risk assets relative to fixed income.

Financial companies are particularly exposed to changes in credit demand, asset quality and the shape of the yield curve. Consumer-oriented businesses are sensitive to household financing conditions and disposable income. Infrastructure, utilities and other capital-intensive industries depend heavily on long-term financing costs and regulatory stability.

Export-oriented and commodity-related sectors respond differently. Their revenues depend more heavily on global prices, external demand and the exchange rate, which may partially insulate them from domestic political cycles. This provides the Brazilian equity market with an important external component that differentiates it from economies more dependent on domestic demand.

| Commodities Remain a Structural Anchor

The country remains a major global producer of agricultural products, energy and minerals. These sectors provide Brazil with a structural connection to global commodity cycles and generate significant export revenues.

Favorable external conditions can therefore partially offset domestic weakness, while an adverse commodity cycle can reduce the benefits of improvements in local policy. This characteristic has historically allowed Brazilian assets to respond simultaneously to two distinct forces: domestic political and fiscal conditions on one side, and global commodity demand on the other.

| What Markets Should Watch After the Election

The initial reaction following the first round and potentially a second round, may be significant, but the sustainability of any repricing will depend on the signals that follow the election.

- The first variable will be the fiscal framework. Markets will need to determine whether the new administration can present a credible path toward stronger primary balances and eventual debt stabilization.
- The second will be the composition of the economic team and the degree of institutional continuity in fiscal and monetary policy. Clear communication regarding fiscal objectives could reduce uncertainty, while inconsistencies between expenditure commitments and fiscal targets could keep the risk premium elevated.
- The third will be governability. The composition of Congress will determine how much of the winning program can be implemented and how quickly structural reforms can advance.

Variable	Strong Fiscal Credibility	Gradual Continuity	Fiscal Deterioration
Fiscal policy	Credible path toward stronger primary balances and debt stabilization	Existing framework maintained; results depend on expenditure control and fiscal targets	Spending pressures weaken expected primary balances and debt dynamics
Sovereign risk and long-term rates	Risk premium and long-term yields could decline	Could remain broadly stable if fiscal targets retain credibility	Risk premium and long-term yields could rise
Brazilian real	Lower sovereign risk could support the currency	Remains sensitive to fiscal signals and external conditions	Depreciation pressure and exchange-rate volatility could increase
Inflation and monetary policy	Better expectations could make monetary easing more effective	Easing remains gradual and dependent on inflation	Exchange-rate pressure could add to inflation and limit room for rate cuts
Brazilian equities	Lower discount rates could support valuations, particularly in domestic sectors	Performance varies by sector and financing conditions	Higher discount rates could weigh on domestically exposed sectors
Commodity exporters	Global prices, external demand and the exchange rate remain key drivers	Global prices, external demand and the exchange rate remain key drivers	They may prove relatively more resilient than domestic sectors, depending on external conditions

Finally, investors will need to distinguish short-term political volatility from changes in Brazil's longer-term fundamentals. Commodity exposure, a large domestic economy, substantial productive capacity and a developed financial system remain structural characteristics independent of the electoral cycle.

| After the Election

Brazil's October election is an important event for financial markets, but its ultimate relevance will be determined less by the political result itself than by the economic framework that follows.

The central challenge facing the next administration will be to reconcile economic growth, and social and investment priorities with the need to stabilize public debt. Brazil's elevated interest burden makes this particularly important because fiscal credibility, inflation expectations and monetary policy are increasingly interconnected.

The two economic-policy frameworks analyzed propose different mechanisms for addressing this challenge. A continuity scenario emphasizes the existing fiscal framework, revenue measures, expenditure control and investment-led growth. An alternative framework emphasizes redesigning fiscal rules around debt stabilization, expenditure restraint, administrative reform and greater private-sector participation. In either case, implementation and congressional support will determine whether fiscal objectives translate into actual improvements in debt dynamics.

Ultimately, the most important market question is not simply who governs Brazil after 2026, but whether the next administration can create the conditions for the country's risk premium to structurally decline.

This opinion article was written on September 30, 2026, by the analyst team at OTG Asset Management.

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