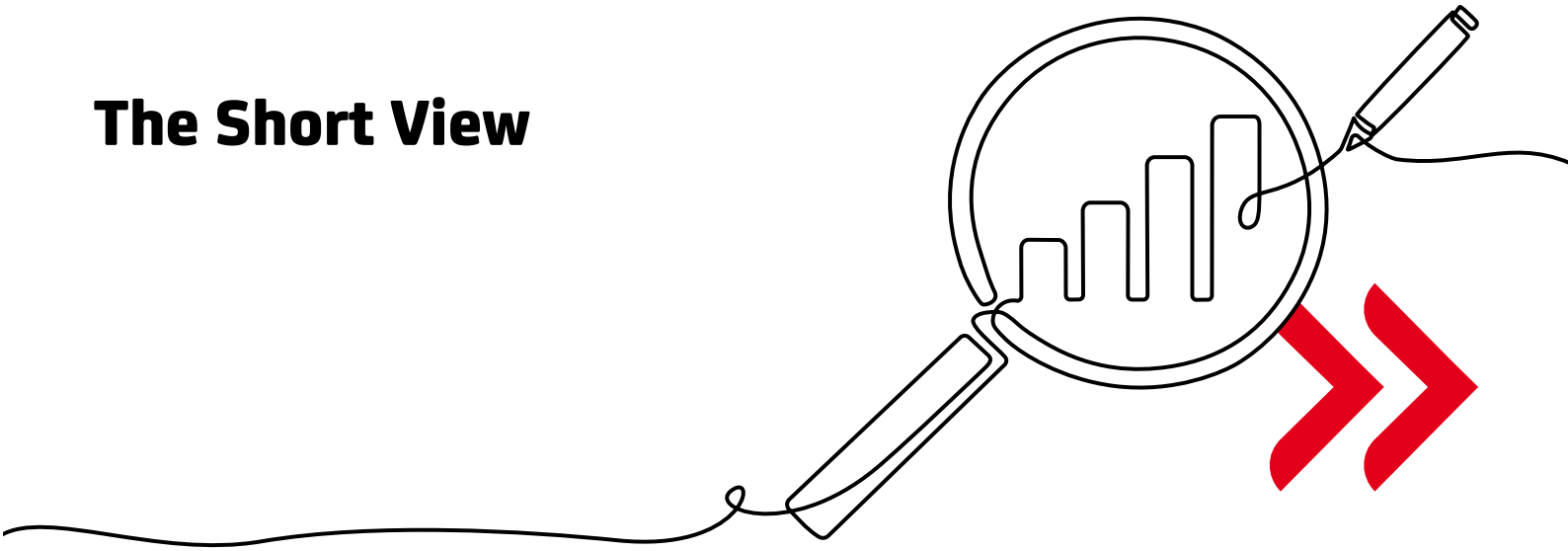
The Short View



The Short View offers insights on key macro and market stories and is designed to promote discussion and debate.

BRL approaching a crossroads at the 25 October runoff

13 October 2026

The BRL appreciated sharply against both the USD and the EUR as, contrary to pre-election polls, Flavio Bolsonaro finished ahead of President Lula da Silva in the first round of Brazil's presidential election. The BRL's response to the 25 October runoff will depend on the winner: if Bolsonaro wins, USD-BRL may even fall below 4.80; if Lula wins, it will likely rise back towards 5.20 or higher. Moves in EUR-BRL are likely to be even larger, although their magnitude will also depend on EUR-USD dynamics.

1. **The event:** The Brazilian real strengthened sharply against both the USD and the EUR following the first round of Brazil's presidential election held on 4 October. Contrary to pre-election polls, the right-wing candidate Flavio Bolsonaro came out ahead of President Inácio Lula da Silva.
2. **The picture:** In turn, this heightens market interest in the runoff scheduled for 25 October. The first-round result was very close (47% for Bolsonaro vs. 45% for Lula), while the abstention rate remained high at over 20%. Turnout could therefore influence the outcome of the second round.
3. **Our view:** The reaction of the BRL to the runoff is straightforward: if Bolsonaro wins, the BRL could extend its rally, dragging USD-BRL below May's low of 4.88 and potentially to 4.80 and even below. If Lula claims victory, the BRL is set to give back its recent gains and a return to pre-election levels around 5.20-5.30 is possible. EUR-BRL will likely be exposed to larger fluctuations, while also being influenced by EUR-USD movements.

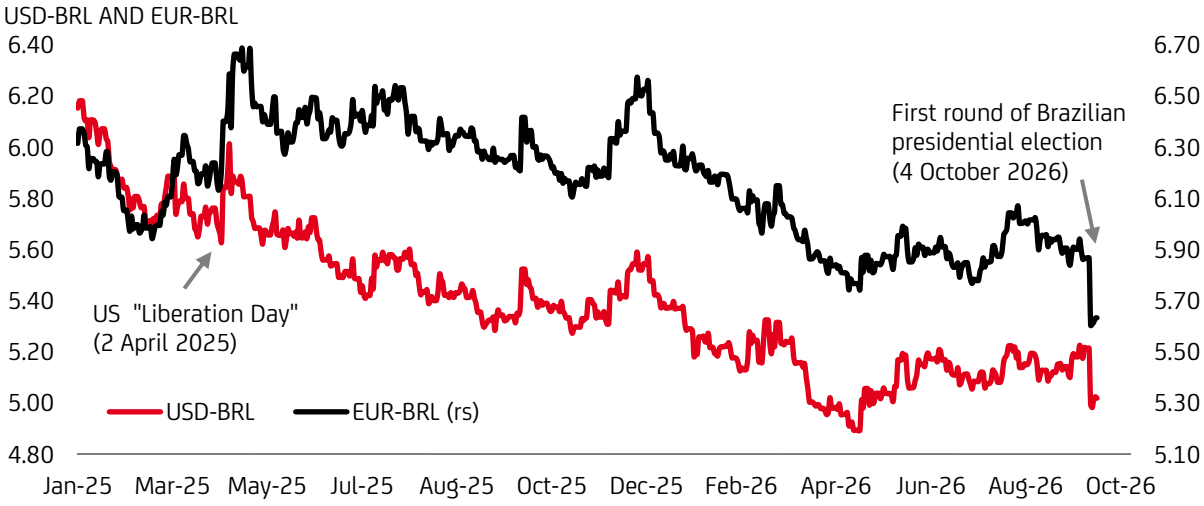
The Brazilian real (BRL) rallied sharply against both the USD and the EUR following the first round of the Brazilian presidential election, which was held on 4 October. This was because, contrary to pre-election polls, the right-wing candidate Flavio Bolsonaro, son of former President Jair Bolsonaro, finished ahead of the incumbent left-wing President Lula da Silva.

The market reaction was impressive: the Brazilian stock market jumped by over 7% and the BRL appreciated sharply against both the USD and the EUR.

As shown in Chart 1, USD-BRL opened on 5 October marking a huge gap compared to the close level of on 2 October, the last trading days before the first round. It dropped 4.5% to 4.9762, down from 5.2132 and then reached a daily low of 4.9523 before consolidating around the 5.00 handle in the following days.

The EUR-BRL reaction was even more intense, due to the simultaneous fall in EUR-USD below 1.12, which amplified the appreciation of the Brazilian currency. The pair tumbled 5.5% from 5.8664 at the close on 2 October to a low of 5.5417, before steadying back above 5.62 over the remainder of the week.

CHART 1: THE REAL APPRECIATED SHARPLY AS BOLSONARO BEAT LULA IN THE FIRST ROUND



Source: LSEG, the Investment Institute by UniCredit

BRL strength: the story so far and the reasons behind it

Brazilian financial markets reacted very well to Bolsonaro's first-round victory, which consolidated the right-wing party's influence in parliament and at the local governor level.

This is because Bolsonaro presented a programme of strong fiscal discipline, in contrast to Lula's policy of sharply increasing fiscal spending, which has pushed Brazil's debt to a high, though not extreme, level of 83% of GDP. Bolsonaro pledges tighter control of public finances through spending cuts and a cap on public debt growth. He also promises a sharp pivot on corruption, climate and the Amazon rainforest.

It is worth noting that over the past year and a half, the BRL has proven to be one of the strongest currencies in the world, not just among emerging-market units, appreciating against the USD even during periods of US dollar strength.

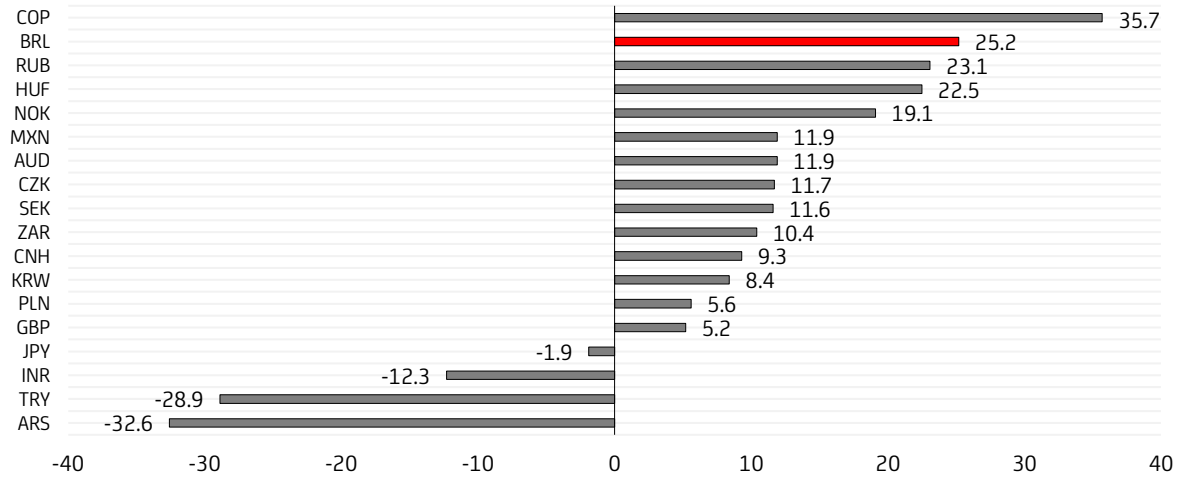
This is visible in Chart 2, which plots spot returns (in percentage points) against the greenback for major developed- and emerging-market currencies since December 2024. The BRL has proven to be the second-strongest currency against the USD, after the Colombian peso (COP).

The BRL fell in the aftermath of "Liberation Day" (2 April 2025), when US President Donald Trump announced heavy duties on imports from major US trading partners, including Brazil, whose exports faced a 50% tariff.

Since then, however, the BRL has steadily strengthened against the USD. USD-BRL fell from above 6.30 in December 2024 to around 4.88 last May, representing BRL appreciation of over 25%.

CHART 2: THE BRL HAS PROVEN THE SECOND STRONGEST WORLD CURRENCY VS. THE USD SINCE LATE 2024

SPOT RETURNS AGAINST THE USD IN PERCENTAGE POINTS FOR MAJOR WORLD CURRENCIES SINCE DECEMBER 2024



Source: LSEG, the Investment Institute by UniCredit

The extremely restrictive monetary policy conducted by the Banco Central do Brazil (BCB) also contributed to the appreciation of the BRL. The BCB kept the key monetary policy rate, the Selic rate, at very high levels, up to 15%, to curb domestic inflationary pressures.

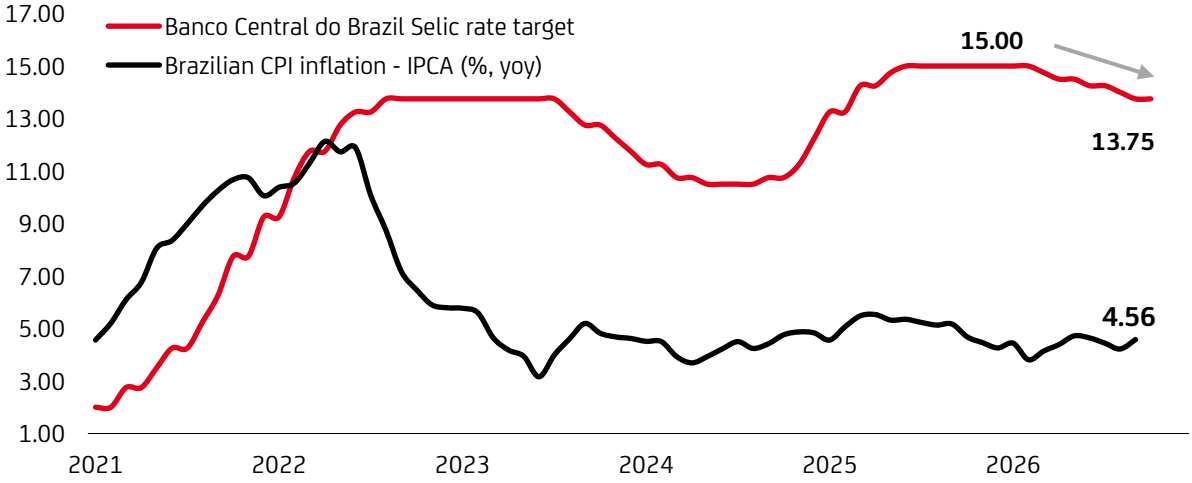
This also increased the BRL's appeal as an investment currency, particularly for carry trades. Carry-trade appeal is also one of the main reasons behind the COP's even stronger performance.

The Brazilian central bank only began lowering the Selic rate at the beginning of this year, with the last 25bp cut to 13.75% coming on 16 September (see Chart 3 below). At present, regardless of the outcome of the presidential election, no further changes to interest rates are expected in the near term.

The Brazilian trade surplus also remains solid, at around 3% of GDP, and this, too, has contributed to the currency's appreciation.

CHART 3: VERY TIGHT MONETARY POLICY AT HOME CONTRIBUTED TO THE BRL STRENGTH

BCB SELIC RATE AND BRAZILIAN IPCA CPI INFLATION



Source: LSEG, the Investment Institute by UniCredit

Brazil: economic outlook, strengths and weakness in a nutshell

Before assessing the potential impact of the 25 October runoff on the BRL, we review Brazil's current economic outlook, strengths and weaknesses.

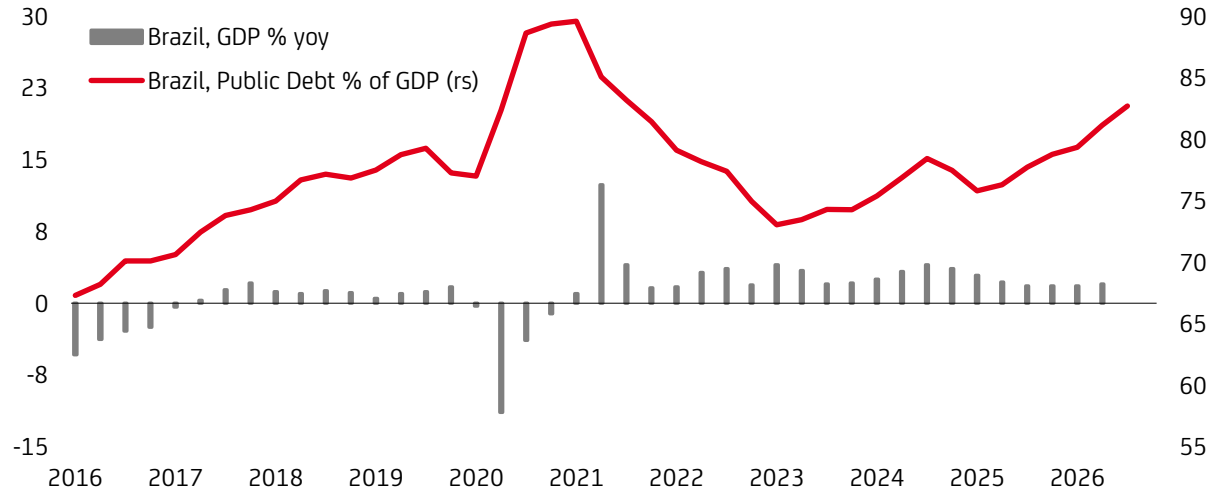
Brazil is currently experiencing moderate but stable economic growth, primarily driven by the commodities sector and robust domestic demand, though held back by high interest rates and still-fragile public finances.

GDP growth is expected to settle at around 2.0-2.4% this year and remain in the 2.0-2.2% range in 2027. Notably, second-quarter Brazilian GDP showed a 1.9% yoy increase (see Chart 4).

IPCA inflation stands at approximately 4.60%, which is still above the central bank's target of 3%. As also showed in Chart 4, the debt burden remains around 83% of GDP and the budget deficit at nearly 9% of GDP, largely driven by interest payments.

CHART 4: BRAZIL STILL STRUGGLING BETWEEN MODERATING ECONOMIC GROWTH AND RISING DEBT BURDEN

BRAZILIAN GDP AND PUBLIC DEBT AS PERCENTAGE OF GDP



Source: LSEG, the Investment Institute by UniCredit

The country's strengths include: **1.** energy independence and transition, given that 90% of Brazil's electricity comes from renewable sources; **2.** the availability of mineral and agricultural resources, as Brazil is a global giant in commodity exports, holding crucial strategic reserves including niobium and lithium and **3.** IMF projections placing Brazil among the world's ten largest economies by 2030.

However, weaknesses remain: **1.** public debt and the high rigidity of government spending, with a large portion of the budget tied to salaries and pensions, limit the government's room for manoeuvre; **2.** double-digit interest rates raise the cost of credit, dampening private investment and domestic industrial activity and **3**. political uncertainty and electoral cycles create market volatility and uncertainty for foreign investors.

The BRL: possible reactions to the 25 October runoff

The short-term outlook for the BRL will inevitably be determined by the outcome of the ballot on 25 October. Notably, Bolsonaro is leading Lula da Silva ahead of Brazil's also in early polls published ahead of the 25 October poll, building on momentum after the surprise emerged in the first-round vote.

In details, Bolsonaro would win about 53% to Lula's 47% of valid votes, excluding blank and invalid ballots, according to a poll for Bloomberg published Friday. If this gap is confirmed by other polls ahead of the 25 October deadline, the BRL may even start reacting in advance, extending its gains beyond the 4.99 threshold against the greenback.

Put simply, a Bolsonaro victory would likely support further BRL appreciation, whereas a Lula victory would be negative for the currency. Sustaining those gains under Bolsonaro would, however, depend on his pledge of fiscal discipline being honoured in practice.

Hence, exporters will need to hedge against the risk of a Lula victory, while importers will need to hedge against the risk of a Bolsonaro victory. Note that three-month implied volatility levels for both USD-BRL and EUR-BRL are currently hovering between 13% and 15%, according to LSEG data.

The implications for USD-BRL and EUR-BRL differ:

1. **USD-BRL:** If Bolsonaro wins, the USD-BRL exchange rate could easily fall below its May low of 4.88 and even test the 4.70-4.80 area. A victory for Lula would obviously yield the opposite result, given the likely continuation of his fiscal spending. In that scenario, a return to at least the 5.20-5.30 range, where the pair traded ahead of the first round, appears inevitable. More critically, such a rebound would bring USD-BRL back into the bullish channel that was in place prior to the election, with a potential target around 5.50.

2. **EUR-BRL:** The EUR-BRL reaction is more difficult to predict as the pair is likely to be exposed to larger fluctuations than USD-BRL. This is because EUR-BRL is a cross rate and is also influenced by EUR-USD movements. The matrix below illustrates potential EUR-BRL values relative to the current rate of approximately 5.60. It combines two run-off scenarios, with USD-BRL at 4.80 following a Bolsonaro victory or 5.30 following a Lula victory, with three EUR-USD assumptions: the current rate (assumed to be 1.12 for simplicity) and UniCredit's current forecasts of 1.14 for 4Q26 and 1.18 for 4Q27. As you can see, the potential EUR-BRL levels vary widely across the different scenarios. The implied exchange-rate risk relative to the current level therefore warrants careful consideration.

TABLE 1: EUR-BRL POSSIBLE VALUES UNDER DIFFERENT USD-BRL AND EUR-USD SCENARIOS

EUR-BRL scenarios (current value at 5.60)	**EUR-USD at current levels** (1.12)	**EUR-USD: UniCredit forecast for 4Q26** (1.14)	**EUR-USD: UniCredit forecast for 4Q27** (1.18)
Bolsonaro wins (USD-BRL at 4.80)	5.38	5.47	5.66
Lula da Silva wins (USD-BRL at 5.30)	5.94	6.04	6.25

Source: LSEG, the Investment Institute by UniCredit

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