Flash

Brazil

COPOM sticks to the “moderate” easing strategy

he Monetary Policy Committee (COPOM) cut the SELIC rate by 50bps to 11.50% as most expected (some few analysts had forecasted a sharper drop). The decision was in line with the monetary authority’s previous communication. The reference to a “moderate adjustment” was included in yesterday’s communiqué and supports our view that the SELIC rate will be cut by extra 50bps in the end of November and will close the year at 11.0%.

- ### Unanimous decision, brief statement and focus on the global environment

  In contrast with the previous cut in the end of August, this time’s decision was unanimous. Also in contrast with the previous meeting, yesterday’s statement was brief: “Continuing the process of adjusting monetary conditions, the COPOM unanimously decided to reduce the SELIC rate to 11.50%, with a neutral bias. The COPOM understands that, in suitably mitigating the effects coming from a more restrictive global environment, a moderate adjustment in the basic interest rate is consistent with the scenario of inflation converging to the target in 2012”. This statement shows that the CB remains more focused on external conditions than on domestic issues.

- ### SELIC at 11.0% by the end of 2011 and at 10.0% by the end of next year

  COPOM’s decision suggests that a more aggressive adjustment of interest rates will only be implemented if global conditions deteriorate very sharply. We, therefore, reinforce our call for another 50bps cut in the last monetary meeting of this year in the end of November. For the next year, the space for additional cuts will be limited by a relatively less supportive fiscal policy (fiscal target to be met this year but not in 2012) and also by the fact that inflation should not converge to the 4.5% target as soon as the CB expects, but the monetary authority should find/create some room for continue cutting the SELIC. We expect it to be at 10.0% by the end of 2012, but see a downward bias in this call, meaning that a one-digit rate should not be ruled out.

- ### Inflation to slow down from now on but not to meet the target in 2012

  Due to a high-base effect, yearly inflation will start to move downwards soon. More precisely, we expect it to decline from 7.3% to 7.0% in October and then to close the year at 6.5%. An activity moderation in both global and domestic fronts will continue driving inflation down in 2012, but a still strong labor market and the usual inertia-related problems of the Brazilian economy will prevent inflation from meeting 2012’s target. We expect it to be at 5.4% at the end of the next year.

For more on Brazil, click here.

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