Brazil Flash

CB forecasts GDP to grow 3.0% in 2011 and 3.5% in 2012

The just-released Inflation Report also sees 2012 inflation around 4.7%y/y-4.8%y/y, which is not very different from previous forecasts in spite of the deterioration of the global economic scenario, the moderation of domestic demand and the re-weighting of the IPCA. We keep our call for the SELIC: two additional 50bps cuts during Q1 12.

- **Economic activity "will continue being supported by domestic demand".**
  Regarding the recent moderation of the Brazilian economy, in our opinion there was room for the CB to provide a more dovish view. The monetary authority highlighted the fact that the economy moderated in Q3 but we saw no important signs of concern with a more prolonged stagnation or with the possibility of the country facing a recession. Quite the opposite: the CB expects the domestic economy to continue growing, driven by the expansion of both credit and income. Regarding the external environment, the CB expects now the "more restrictive" tone of the global economic environment to "remain during a more prolonged period than expected". "Extreme events", however, are not incorporated in CB's base scenario. Taking all together, the CB forecasts GDP to grow 3.0% in 2011 and 3.5% in 2012, broadly in line with BBVA and markets expectations.
- **Lower inflation in 2012, but still above the target**
  The CB revised 2011 inflation to 6.5%y/y from 6.4%y/y. More importantly, it revised 2012 inflation forecasts to 4.7%y/y (base scenario in which the SELIC and the real constant at 11.0% and 1.80, respectively) and 4.8%y/y (market scenario which takes into account markets expectations for both the SELIC and the exchange rate) from 4.7%y/y and 4.9%y/y. Its is worthwhile noting that the new forecasts are not very different from the previous ones in spite of the monetary authority having incorporated the re-weighting of the IPCA, the perspectives of global and domestic moderation and lower risks of labor markets putting excessive pressure on inflation. In any case, the CB's inflation forecasts remain significantly lower than BBVA and markets expectations (both around 5.4%y/y).
- **Not as dovish as it could have been.**
  Given the contraction of domestic demand in Q3, the re-weighting of the IPCA which could drive official inflation down around 30bps and the deterioration of the external environment, many could have expected a more dovish Inflation Report. The document provides, therefore, extra support to the view that additional SELIC cuts will be of 50bps instead of 75bps. We expect two additional 50 bps cuts and, therefore, the SELIC to reach 10.0% by the end of Q1 12. Although we attach a higher probability for the CB keeping interest rates stable at 10.0% from the end of the first quarter on, additional cuts should not be ruled out.

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