Brazil Flash

Unemployment and inflation surprise to the downside

The unemployment rate reached 5.7% in February, the lowest rate for the period and slightly below market expectations (5.9%). Wages continue increasing at a solid pace, which reinforce the view that labor markets continue vibrant. Mid-March IPCA-15 inflation was also released today: it came out at 0.25%m/m, significantly less than the consensus expected (0.38%m/m).

- **Labour markets remain tight…**

  The unemployment rate continued very close to historical lows. The seasonally adjusted series shows that unemployment dropped from 5.7% in January to 5.6% in February, which is just a decimal point higher than the historical low recorded in the end of 2011. Seasonally adjusted wages grew 4.6%y/y (1.0%m/m) in real terms in February, which is more than the average observed in 2011 (2.7%y/y; 0.2%m/m). Labor markets, therefore, continue strong in spite of the recent economic deceleration. Even though we would not be surprised if they lose dynamism in the months ahead, labor markets will certainly be among the main supporters of the activity recovery we expect for the year.

- **… and, in spite of the recent deceleration, inflation continues well above target…**

  IPCA inflation dropped to 5.9%y/y in February from 6.5%y/y in December. And Mid-March IPCA-15 inflation – which measures inflation from Feb 15 to March 15 - came out today at 5.6% y/y (0.25%m/m), less than in the previous reading (6.0%y/y; 0.53%m/m) as food prices continued decelerating and seasonal effects provided important support. In spite of this moderation –at a large extent due to significant base effects- inflation remains significantly above the 4.5% target. Even though this downward trend will continue in the next few months, inflation will continue in the 5.0% - 6.0% range for a long period. More precisely, we expect headline inflation to close 2012 at 5.4%y/y and 2013 at 5.6%y/y. And the risks are (increasingly) to the upside.

- **Monetary easing will, however, continue till the SELIC reaches 9.0%**

  Another element for seeing upside risks to our inflation forecasts is the renewed dovishness of this Central Bank Board, which surprised markets some days ago by cutting the SELIC by 75bps (instead of 50bps) and making practically explicit its idea to bring rates to 9.0% soon. We, therefore, revised our call for the SELIC and expect now a last 75 bps cut in the next monetary policy meeting in April and, then, a very long pause at 9.0% (not anymore at 9.50% as we expected before).

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