Brazil Flash

No country for hawkish men

Brazil's CB decided to cut the SELIC rate by 75bps to 9.0%, in line with expectations. However, the accompanying statement suggested that the easing cycle may have not ended yet as many - including BBVA Research - expected.

- **"Limited risks for the inflation path"**

  The decision to cut the SELIC from 9.75% to 9.0% was unanimous. After this downward adjustment the SELIC is now 350bps lower than in August of 2011, when the easing cycle started. Since then, the Monetary Policy Committee (COPOM) of the Central Bank has been constantly looking for room to bring the SELIC down. The dovish tone is already a trademark of this COPOM. In the communiqué released yesterday, the monetary authority kept the focus on the ("disinflationary") external environment and referred to lower inflationary risks: "The COPOM considers that at this moment there are limited risks for the inflation path. The Committee also notes that, up to now, the contribution of the external sector has been disinflationary, given the fragility of the global economy. Therefore, continuing the monetary adjustment process, the COPOM decided, by a unanimous vote, to reduce the SELIC to 9 percent per year, without bias."

- **Downward risks to interest and inflation rates in the short-term…**

  As yesterday's communiqué suggests, the chances of the CB cutting the SELIC again (by 50bps or 25bps) in its next meeting in May are non-negligible. We see, therefore, a clear and relevant downside risk to our current call for the SELIC (9.0% till the end of the year), especially if the external scenario remains turbulent and inflation continues surprising positively. The release of the minutes of the most recent COPOM meeting next week should shed some light on the issue. With respect to inflation, even though we see room for it to continue surprising to the downside and dropping in yearly terms in the next few months (it declined already from 6.5%y/y in December to 5.2%y/y in March), we continue expecting it to respect the 5.0% barrier and to close the year around 5.4%.

- **…and upside risks in the longer-term**

  If, on one hand, the risks to inflation and interest rates are to the downside in the short-term (2012), on the other hand, we see upside risks in the longer-term (2013). The activity recovery we expect for the rest of the year and for 2013, and which will be especially driven by a lax monetary policy, puts an upside bias to our 2013 inflation forecasts (average: 5.8%; end-of-period: 5.7%) and, therefore, to our 2013 SELIC call (rates constant at 9.0%).

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