

Brazil Flash

Government adopts a new scheme to remunerate saving accounts and eliminates a barrier for moving the SELIC down

The government decided to face the political costs of changing the rules governing the remuneration of the *poupança* (the most popular form of savings accounts in the country) by announcing measures that, in practice, will create room for the SELIC to continue moving downwards. We now expect the SELIC to soon reach 8.25% and see higher inflationary risks in the medium-term (especially in 2013).

- **The return on *poupança* accounts will now be linked to the SELIC**

Late on Thursday, the Minister Guido Mantega announced that the previous remuneration scheme (0.5% per month plus a small monetary correction) will be replaced by a new scheme in which savers will get 70% of the SELIC plus the same small monetary correction in the case the SELIC is below 8.5%. The previous remuneration scheme will remain if the case the SELIC is equal or above 8.50%. The new rules for the *poupança* will only be valid for new investments and will continue being tax-free.

- **A positive change, with political costs**

We see the change announced yesterday as positive because it puts an end to an antiquated rigidity, inherited from inflationary times, and creates more space for monetary policy. It, however, has a political cost as the nominal returns of this popular and very traditional form of saving accounts can decline from now on. The political costs of such initiative can, actually, be illustrated by the widespread opposition to the changes suggested in 2009 (in line with the changes announced yesterday) by the former President Lula. The President Dilma certainly expects the political benefits of lower interest rates to offset the political costs of altering saving accounts returns.

- **Perspectives of lower interest rates and higher inflation**

Even though the new regulation is a positive step from the structural point of view, it is not necessarily positive from a macroeconomic point of view as, at this moment, it can trigger "excessive" interest rate cuts and add to medium-term concerns with inflation. As in our view the "saving accounts barrier" -and not inflation- was the main obstacle for moving the SELIC further down, we now expect the CB to bring rates to 8.25% by delivering a 50bps cut in the end of May and a final 25bps cut in July. We then expect rates to remain stable at that level till the end of the year. As a consequence of a laxer than expected monetary policy, we see now higher pressures on inflation in the second half of this year and, especially, in 2013 when inflation would near 6.0%.

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