

Brazil Flash

Monetary policy minutes: a more hawkish tone, still in line with the stability of monetary conditions

In the monetary policy minutes released today, the COPOM recognizes that the balance of risks for inflation has deteriorated, especially in the short-term. The monetary authority now sees inflation above target through 2013 and 2014. Rising inflation and the correspondent change in the tone of monetary policy have practically closed the door to a SELIC cut and triggered talks about an upward adjustment. Even though a SELIC hike should not be ruled out, we continue to see more likely the stability of interest rates at 7.25% for a “prolonged period of time”.

- **Focus has shifted from external uncertainty to domestic issues**

The diagnosis of the external environment remained practically unchanged (“risks regarding the global financial stability remain high”), but the COPOM’s main focus is now on the domestic front. Both the worsening of the balance of risks for inflation and lower than expected economic activity were noted, but more emphasis was placed in the former than in the latter. For the COPOM, “the more widespread increases in consumer prices and the reversal of tax exemptions, together with seasonal pressures and punctual pressure in the transport segment, tend to contribute to the resistance of inflation in the short-term”. The monetary authority revised upwards their inflation forecasts and now sees inflation above the 4.5% target in 2013 and “slightly” above that mark in 2014. Regarding administered prices, the minutes reveal that a 5% adjustment in the gasoline price and an overall decline of 11% in household electricity tariffs are expected and incorporated in its forecasts for 2013. With respect to domestic activity, the minutes referred to lower than expected growth due to “limitations in the supply side” (“which, given their nature, cannot be addressed by monetary policy actions”) and the “weakness of investment” (“which reflects, to a large extent, the increase in uncertainty and the slow recovery in confidence”).

- **The announcement of deeper than previously indicated cuts in electricity tariffs shows that tools other than the SELIC will be used to control inflation**

The IPCA-15 for January, which measures inflation from mid-December to mid-January, reached 6.0%YoY (0.9%MoM), revealing that inflation continues to rise at the beginning of the year (see our [Brazil Flash](#) for more on this issue). Following the release of this data, President Dilma announced that electricity tariff cuts will be introduced immediately (and not in February as indicated previously) and will be within the 18%-32% range (deeper than expected: 16%-28%). In line with what we have been saying in the last few months, this announcement shows that tools other than the SELIC will be used to prevent inflation from running out of control. Even though electricity tariff cuts will bring some relief, we expect inflation to trend up over the semester and to be close to the upper bound of official inflation target (6.5%) by the middle of the year. However, weak activity growth -and the use of other tools- should, in our view, prevent the BCB from adjusting the SELIC up.

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Acta de política monetaria: un tono más duro, pero todavía en línea con la estabilidad de las condiciones monetarias

En el acta de la última reunión de política monetaria, el COPOM reconoció que el balance de riesgos para la inflación empeoró, especialmente en el corto-plazo. La autoridad monetaria ahora espera que la inflación esté por encima del objetivo tanto en 2013 como en 2014. El aumento de la inflación y el cambio del tono de la política monetaria han prácticamente cerrado la puerta a un recorte del SELIC y alimentado rumores sobre su ajuste al alza. A pesar de que no podemos descartar un aumento del SELIC, seguimos viendo más probable que se mantengan los tipos de interés en 7,25% durante un “período de tiempo prolongado”.

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