ECONOMIC ANALYSIS

COPOM rules out cutting the SELIC

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The minutes of last week's monetary policy meeting released today show that the Monetary Policy Committee (COPOM) remains confident on the convergence of inflation to the target in the "final quarters of the forecast horizon" (i.e. beginning of 2016), in spite of shorter term pressures. More importantly, the monetary authority affirmed that the strategy to ensure this convergence "does not include reducing the monetary policy instrument". This surprisingly explicit statement is in line with our view that any adjustment in the SELIC rate will be to the upside, although very likely only from the beginning of 2015 onwards.

By closing the door to a cut in the SELIC rate the COPOM is trying to anchor inflation expectations

In consonance with its concerns about the dynamics of domestic prices in the short-term, due to factors such as the realignment of administered prices, the expected exchange rate depreciation and wage gains above productivity growth, the monetary authority revised upward its inflation forecasts for 2014 and 2015, in both baseline and alternative scenarios (as usual, the figures were not revealed). However, in spite of these pressures in this and in the forthcoming year, the COPOM highlighted that under the current monetary conditions, inflation tends to converge to the target by the end of the forecast horizon (i.e. in the first half of 2016). Even though this claim supports the view that the SELIC rate will be left unchanged not only over 2014 but also thorough 2015, we think that the normalization of monetary policy in the US, and still high domestic inflation, will force the monetary authority to increase interest rates next year, the first of the new federal government to be elected in October 2014. Regarding the most relevant part of the minutes, i.e. the part where the COPOM practically closed the door to a monetary easing, we see it as way for the monetary authority to recover some credibility and try to anchor long-term inflation expectations.

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