Copom: Steady at the helm

The Copom delivered the widely expected decision, cutting the Selic rate by 50 bps, to an all-time low of 5% p.a., in a unanimous decision. Its statement indicated that the next policy move will probably be another 50 bps cut, taking the Selic to 4.5% p.a. by year-end. The authorities calibrated their communication to curtail market expectations about additional monetary easing, although the forecasts presented, especially that for 2021 inflation in the market scenario (3.5%), suggest they should be comfortable about taking the policy rate to 4% p.a. We expect the Copom to cut the policy rate to 4.5% in its final meeting of the year, and to 4% pa by March 2020. We will learn more about the rationale for this decision with the release of the meeting minutes on Tuesday, November 5, at 08:00 Brasilia time.

Details

The Copom stated that activity indicators released since the last meeting reinforce the continuity of the economic recovery process, and affirmed that their scenario assumes this recovery take place at a gradual pace.

Regarding the external environment, the committee maintained the message that additional monetary stimuli in major economies, in a context of economic slowdown and below-target inflation rates, has been favorable to emerging economies. The Copom considers that the scenario remains uncertain and that the risks associated with a more intense global slowdown persist.

The committee assessed that underlying inflation measures are at comfortable levels, including those most sensitive to the economic cycle and monetary policy.

Focus survey inflation expectations for 2019 and 2020 receded to 3.3% and 3.6%, from 3.5% and 3.8%, respectively, and remained stable at 3.75% for 2021 and 3.5% for 2022.

With regard to Copom’s own forecasts, in the hybrid scenario with constant exchange rate at BRL 4.05/USD and interest rates extracted from the Focus survey, inflation is forecast around 3.4% for 2019, 3.7% for 2020 and 3.6% for 2021.

In the scenario with trajectories for interest and exchange rates extracted from the Focus survey, the Copom forecast oscillated to 3.4% in 2019 (from 3.3%) and remained stable at 3.6% for 2020. For 2021, the inflation forecast is 3.5%. This scenario assumes interest rates trajectories that end 2019 at 4.50% p.a., remains at that level throughout 2020 and increases to 6.38% p.a. by the end of 2021. For the exchange rate, this scenario assumes BRL 4.00/USD by the end of 2019, remaining at that level throughout 2020 and reaching BRL 3.95/USD by the end of 2021.

Regarding the balance of risks for inflation, the Copom continued to highlight that, in its baseline scenario, there are still risk in both directions. On the one hand, the high level of slack and the potential propagation of current inflation by inertial mechanisms may continue to produce lower-than-expected inflation, while, on the other hand, the current degree of monetary stimulus, which, according to the Committee, acts with lags in the economy, increases uncertainty about the transmission channels and may raise the inflation trajectory over the relevant monetary policy horizon. The latter gets more intense if there is a worsening of the external scenario for emerging economies or eventual frustration about the continuity of reforms and necessary adjustments in the economy.

Accounting for all considerations above, the Copom assessed that the evolution of the baseline scenario and the balance of risks prescribed a 50-bp adjustment in the degree of monetary stimulus. The Committee also maintained
the indication that the consolidation of the benign scenario for prospective inflation should allow a further adjustment of equal magnitude in this degree of stimulus. The Copom also mentioned that the current stage of the economic cycle prescribes caution in any further adjustment in the degree of monetary stimulus and continued to reiterate that such communication does not bind their next decisions.

Therefore, the Copom delivered the widely expected decision, cutting the Selic rate by 50 bps, to an all-time low of 5% p.a., in a unanimous decision. Its statement indicated that the next policy move will probably be another 50 bps cut, taking the Selic to 4.5% p.a. by year-end. The authorities calibrated their communication to curtail market expectations about additional monetary easing, although the forecasts presented, especially that for 2021 inflation in the market scenario (3.5%), suggest they should be comfortable about taking the policy rate to 4% p.a. We expect the Copom to cut the policy rate to 4.5% in its final meeting of the year, and to 4% pa by March 2020. We will learn more about the rationale for this decision with the release of the meeting minutes on Tuesday, November 5, at 08:00 Brasília time.

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