

# Brazil Central Bank Preview: October 2022

**Monetary policy decision and Copom Statement release:** 2230BST / 1730ET, Wednesday October 26, 2022.

## MNI Point of View: Unanimous Hold

After holding rates in September, the consensus view remains that the Copom has ended its tightening cycle. Despite two members voting for a 25bp hike at that meeting, MNI expects a unanimous decision to keep rates unchanged this week at 13.75% as both IPCA readings and inflation expectations continue to moderate.

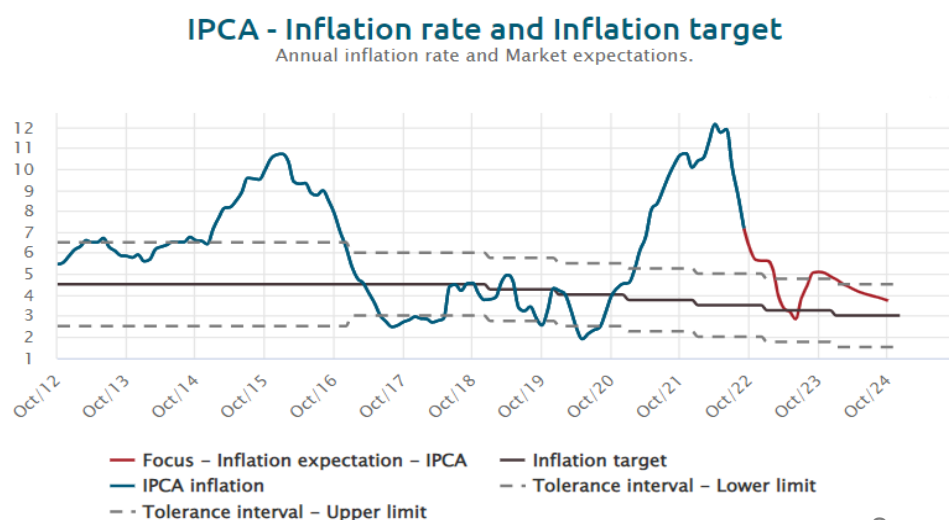
With the global inflation outlook remaining difficult, continued hawkish rhetoric from the central bank should accompany the decision. Additionally, domestic uncertainties relating to this Sunday's second-round presidential election vote and associated concerns around the fiscal trajectory provide solid evidence of needing to maintain the restrictive stance. Updated inflation forecasts may also provide some clues as to when the Copom might begin monetary easing next year.

### Disinflation Process Continues, Expectations Are Easing

October IPCA headline inflation saw another notable decline to 7.17%, marginally above the surveyed median estimate of 7.12% but considerably below the September reading of 8.73%. Furthermore, the latest BCB Focus Survey has seen forecasts be further adjusted to the downside, with year-end 2022 estimates now sitting at 5.60%. This is down from the 6.00% prediction before the September meeting. Additionally, year-end 2023 expectations have also declined, falling from 5.01% to 4.94%, continuing the improvement of medium-term expectations.

It was previously noted that these declines, while welcomed, had been largely as a result of large fuel/electricity/telecom tax cuts and ex-refinery gasoline price declines. Furthermore, stubborn core inflation metrics had made it more difficult to gauge the improvements. However, analysts are starting to indicate that despite services inflation pressures remaining high, core measures and industrial inflation are beginning to show signs of moderation at the margin. Despite the weaker than expected Aug IBC-Br real activity data, Focus has seen marginal improvements for growth; now expecting 2.76% GDP in 2022. The central bank's survey continues to suggest the Selic rate will end this year at 13.75% and then end 2023 at 11.25%, both unchanged from before the September meeting.

**Figure 1: Headline Inflation Shows Steep Moderation In Recent Months**



Source: Brazil Central Bank

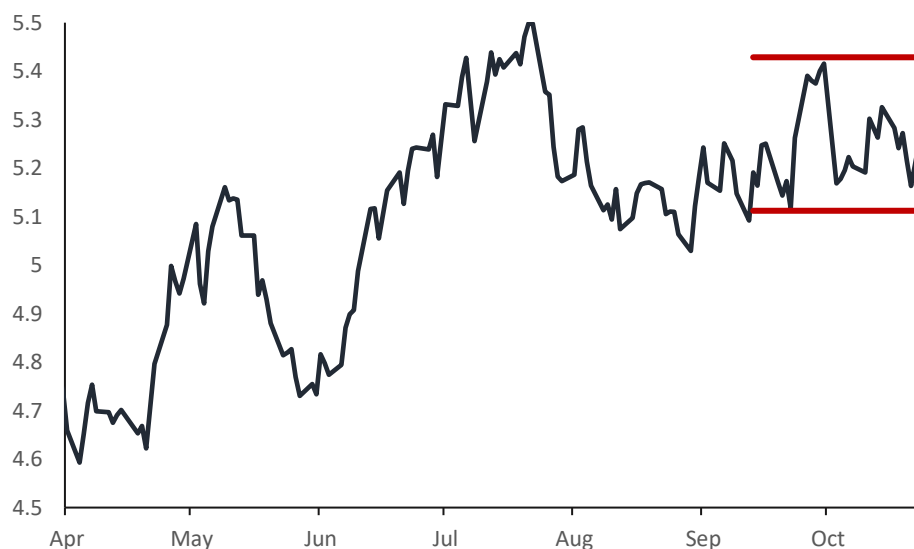
### Any Guidance In Focus For Front-End DI Swap Rates, BRL Fundamentals Balanced

With markets trying to pin-point the expected timing of cuts in 2023, any guidance within the Copom statement, alongside the updated inflation forecasts, will be analysed to assess the Copom's potential desire to maintain the restrictive stance throughout next year. For the currency, short-term factors including global risk sentiment and the upcoming runoff vote outcome are likely to have larger impact.

The most recent narrowing of polling gaps continues to cloud the political outlook and Brazil has already seen episodes of social unrest in recent days, weighing on the Brazilian Real. Furthermore, uncertainty relating to the fiscal trajectory in 2023 amid the continued strength of the USD appear to be the main obstacles from the psychological 5.00 mark in USDBRL giving way. While lingering uncertainties provide obvious BRL headwinds, the combination of high carry and low exposure to the most notable sources of economic distress in Europe keep the fundamental arguments finely balanced.

Technically, attention is on resistance at 5.4286, the Sep 29 high. A break of this level would expose 5.5142, the Jul 21 high and a key resistance. On the downside, key short-term support has been defined at 5.1121, the Oct 4 low. A break lower would instead highlight a bearish development.

Figure 2: USDBRL Short-Term Parameters In Place



Source: MNI/Bloomberg

# mni Central Bank Watch - Brazil

## MNI Brazil Central Bank Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
CPI	% y/y	7.2	11.9	↓	11.3	↓					-0.54
Core CPI	% m/m	0.4	1.0	↓	1.0	↓					-1.81
Oil Price (WTI Active)	\$	83.85	95.56	↓	89.60	↓					-1.59
Economic Activity		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
PMI Manufacturing	Index	51.1	54.1	↓	52.3	↓					-0.72
GDP	% q/q	1.2	0.1	↑	3.2	↓					-0.26
Industrial Man Prod	% y/y	2.8	0.5	↑	-4.1	↑					1.37
Economic Activity IGAE	% y/y	4.86	3.72	↑	1.14	↑					1.46
Monetary Analysis		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
M2 Money Supply	% y/y	4723.7	4528.4	↑	4271.0	↑					2.03
Non-Fin Corp Credit	% y/y	175.0	179.4	↓	180.2	↓					-1.24
Household Credit	% y/y	34.1	32.4	↑	31.5	↑					1.28
Consumer / Labour Market		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
Retail Sales	% m/m	-0.1	-1.9	↑	1.3	↓					0.08
Consumer Confidence (Q)	Index	89.0	79.0	↑	74.8	↑					2.01
Unemployment Rate	%	8.9	9.8	↓	11.2	↓					-1.26
Markets		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
Ibovespa	Index	116,013	98,542	↑	119,999	↓					0.13
Jan 2032 DI Swap Rate	%	11.95	12.89	↓	11.54	↑					-0.65

Note: For quarterly data the 3m ago column will display the previous data point and the 6m ago column will display the data point prior to that.  
Source: MNI, Bloomberg

## Analyst Views (Alphabetical Order):

All 44 estimates provided to the Bloomberg Survey forecast the Selic rate to be left unchanged at 13.75%.

### Barclays: Expect The First Selic Cut In June 2023

- Barclays expect another “hawkish hold” at the Copom’s October meeting, with the Selic rate kept at 13.75%. The post-meeting statement is likely to reinforce the board’s “vigilance” and commitment to maintaining the Selic rate at high levels for a sufficiently long period in order to ensure the convergence of inflation to its targets.
- Concerns about core inflation, particularly in underlying services amid a robust labor market, may be used to justify the hawkish stance, with the communique possibly repeating September’s warning that the BCB “will not hesitate to resume the tightening cycle if the disinflationary process does not proceed as expected.”
- Barclays expect the first Selic cut in June 2023.

### Bank of America: Message Of Rates AT Current Level For Longer To Remain

- BofA expect the Copom to maintain the Selic Rate at 13.75% in its October meeting (after pointing towards the end of the tightening cycle on the last meeting).
- The lagged effects of the monetary tightening cycle and the convergence of expectations closer to the upper band of the target for the relevant horizon for the BCB (2023 and 2024) support our view that BCB's next move will be a cut, but only next year.
- The main message should remain from the last meeting, pointing that rates will remain at the current level for longer.

**Goldman Sachs: Case For Preserving Restrictive Stance Is Justified**

- Given the recent macro-financial developments and the guidance provided at the Sep meeting, Goldman Sachs expect the Copom to leave the Selic policy rate unchanged at a restrictive 13.75% coupled with hawkish/conservative guidance indicating that (1) the Copom will remain vigilant and evaluate if the strategy of keeping the policy rate at the current level for a sufficiently prolonged period of time will be able to secure convergence of inflation to the target, and (2) will not hesitate to resume the hiking cycle in case the disinflation process/path does not evolve as expected.
- The case for preserving a clearly restrictive stance is justified given still intense services and core inflation pressures, solid real activity and labor market dynamics, high uncertainty around the fiscal stance and fiscal rule/anchor in 2023 and subsequent years, signs of sticky global inflation, higher global core yields, and hawkish FOMC and global monetary winds.
- In the post-meeting policy statement, GS will be paying particular attention to the forecasts for year-end 2023 vis-à-vis the 3.25% target, since in its reaction function the Copom is now mostly focused on the 2023 target, and also the forecasts for year-end 2024 vis-à-vis the 3.0% target since the 2024 target will now have a small but gradually larger weight in the central bank reaction function.
- These forecasts and the overall balance of risks for inflation will be key to calibrate the Selic rate path, in particular the room for policy easing in 2023.

**JPMorgan: Continue Expecting The Easing Cycle To Start In June 2023**

- The conditions needed for a change in BCB's posture remain distant. Therefore, the overall message should be of continuity of the policy rate at 13.75% for a prolonged period. BCB seems to be aiming at avoiding signals that would prematurely ease financial conditions, thus JPMorgan don't anticipate meaningful changes to the communication.
- They expect two things to be different from the last meeting. First, the decision to keep rates on hold will likely be a consensus among COPOM members whereas the last decision was split. Second, as happened last year, BCB should now assign equal weights to its forecasts for 2023 and 2024, instead of giving a larger weight to next year. They don't expect meaningful changes to the characterization of the domestic and global scenarios.
- JPM continue expecting the easing cycle to start in June next year—a date that was even explicitly mentioned by Governor Campos recently.

**Scotiabank: Political Considerations Likely To Influence Communications**

- Brazil is in the regional spotlight this week with October inflation data, the BCB's policy decision, and a highly contested second round election on the 30th that will keep markets on edge. Polls in the aftermath of the first-round vote in early-October had held steady in favour of a victory for former President Lula until recently, but recent surveys have moved within the margin of error—and 'hidden' Bolsonaro voters may still come out en masse to support the incumbent.
- The BCB is expected to stand pat for the second consecutive time as its hiking cycle seems to have the intended impact on inflation—with political considerations also likely to influence their communications.

**SocGen: Now See Only ~15% Probability Of An Additional Rate Hike**

- Several developments may be noted since the last Copom. 1) The disinflation process continued in September (and probably in October too). 2) Crude oil prices have stopped falling (up about 2.5% since the last Copom), leading to the misalignment of domestic and global oil prices. 3) The global inflation outlook remains difficult while financial conditions continue to tighten led by the Fed's rate hikes. 4) The BRL has fluctuated in a narrow range and remains on a broadly stable trajectory. 5) Domestic growth and the labour market conditions continued to make robust progress in 3Q22. 6) Political and policy uncertainties have only gone up since the first round of the presidential elections.



- While the disinflation process continues for now, uncertainty over the inflation outlook (both in near and medium terms) has not disappeared. The labour market and growth remain firm while commodity prices could turn a corner again.
- The fiscal outlook is not clear as of now, but it could remain a key source of upward pressure on prices. Overall, the fact that inflation has remained above the BCB's target over the entire policy horizon could be a big factor in deciding the BCB's policy stance going forward.
- Both ex-post and ex-ante real interest rates are now much higher than at any other time in recent years. In fact, the ex-post real interest rate is already twice as high as the BCB considers to be a neutral level. Therefore, the BCB is very unlikely to move towards further tightening unless it sees a clear risk of the disinflation process reversing.
- SocGen continue to believe that the next BCB move will be a rate cut starting in 1Q23 (about 50% probability, 35% in 2Q23, 10% in 3Q23 and 5% in 4Q23). At the same time, we now see some upside risk to our rate expectation of 12.75% in 1Q23.
- A flatter easing cycle to begin with in 1Q23 could develop into steeper rate cuts in 2Q23-3Q23, assuming that inflation continues to moderate in these quarters. For now, SG continue to see the end-2023 Selic rate at 10.75%.