



# BANCO CENTRAL DO BRASIL

## Minutes of the 142<sup>nd</sup> Meeting of the Monetary Policy Committee (Copom)

### Summary

Recent Economic Developments  
Assessment of Inflation Trends  
Monetary Policy Decision  
Inflation  
Economic Activity  
Surveys and Expectations  
Labor Market  
Credit and Delinquency Rates  
External Environment  
Foreign Trade and International Reserves  
Money Market and Open Market Operations

**Date:** April 28<sup>th</sup>, from 5:50PM to 8:10PM, and April 29<sup>th</sup>, from 5:30PM to 7:40PM

**Place:** BCB Headquarters meeting rooms - 8<sup>th</sup> floor on April 28<sup>th</sup> and 20<sup>th</sup> floor on April 29<sup>th</sup> – Brasília – DF

### In attendance:

#### Members of the Committee

Henrique de Campos Meirelles – Governor  
Alexandre Antonio Tombini  
Alvir Alberto Hoffmann  
Anthero de Moraes Meirelles  
Antonio Gustavo Matos do Vale  
Maria Celina Berardinelli Arraes  
Mário Gomes Torós  
Mário Magalhães Carvalho Mesquita

#### Department Heads (present on April 28<sup>th</sup>)

Adriana Soares Sales - Department of Banking Operations and Payments System  
Altamir Lopes – Economic Department  
Carlos Hamilton Vasconcelos Araújo – Research Department (also present on April 29<sup>th</sup>)  
João Henrique de Paula Freitas Simão – Open Market Operations Department  
Márcio Barreira de Ayrosa Moreira – International Reserves Operations Department  
Renato Jansson Rosek – Investor Relations Group

#### Other participants (present on April 28<sup>th</sup>)

Alexandre Pundek Rocha – Advisor to the Board  
Eduardo José Araújo Lima – Advisor to the Research Department  
Flávio Pinheiro de Melo – Advisor to the Board  
José de Ribamar Oliveira Júnior – Press Secretary  
Katherine Hennings – Advisor to the Board

The members of the Monetary Policy Committee analyzed the recent performance of and the prospects for the Brazilian economy and for the international economy, under the monetary policy framework, which is designed to comply with the inflation targets established by the government.



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### Recent Economic Developments

1. IPCA inflation decelerated from 0.48% in January and 0.55% in February to 0.20% in March. As a consequence, inflation accumulated in the first quarter of 2009 reached 1.23%, decreasing 0.28 p.p. relative to the level registered in the same period of the previous year. In the last twelve months, inflation declined from 5.90% in December to 5.61% in March (4.73% in March 2008). The deceleration of twelve-month consumer price trailing inflation in the first three months of the year mirrored the behavior of market prices, as regulated prices increased. Considering market prices, both prices of tradable goods and non-tradable goods cooled on a twelve-month trailing basis, reaching 6.10% and 6.74%, respectively, in March, down from 6.99% and 7.10% in December 2008, despite the acceleration relative to the levels observed in the same month of the previous year. According to the same comparison basis, the prices of services, whose dynamics tends to show more persistence than that of the prices of goods, increased from 6.39% in December to 6.63% in January and 7.09% in February, and decreased to 6.83% in March (5.11% in March 2008). Preliminary data for April point to consumer inflation above that observed in March. In short, information available suggest that the inflationary cycle observed in the last year has been gradually overcome by a process that should continue to be led by the behavior of market prices, while regulated price inflation should show more persistence.

2. The three main underlying inflation measures calculated by the BCB showed divergent behavior in the first three months of the year. The core inflation by exclusion of household food items and regulated prices increased from 0.27% in January to 0.88% in February, reflecting seasonal factors, and then decreased to 0.25% in March. On the other hand, smoothed and non-smoothed trimmed means core inflation measures showed lower variation, recording 0.42% and 0.44% in January, 0.29% and 0.27% in February and 0.35% and 0.21% in March, respectively. The twelve-month trailing inflation measures changed from 6.09%, 4.82% and 4.92% in December to 6.02%, 4.85% and 4.64% in March, for the core inflation by exclusion, smoothed and non-smoothed trimmed means core inflation, respectively, remaining in levels above the midpoint of the target. Moreover, it bears emphasizing that the behavior of the IPCA diffusion index reduced to 60.2% in March down from 61.7% in December (compared to 58.6% in March 2008).

3. The General Price Index (IGP-DI) inflation changed -0.13% in February and -0.84% in March, down from 0.01% in January. On a twelve-month trailing basis, the IGP-DI inflation decreased from 9.10% in December to 5.86% in March, compared to 9.18% in March 2008. The slowdown of the IGP-DI has reflected the behavior of its main component, the Wholesale Price Index (IPA-DI), which decreased from 9.80% in December to 4.98% in March, on a twelve-month trailing basis (11.39% in March 2008). On its turn, the Consumer Price Index-Brazil (IPC-Br) increased 6.32% (4.52% in March 2008) and, according to the same comparison basis, the Civil Construction National Index (INCC) increased 10.66% (6.69% in March 2008). Regarding the IPA-DI, the inflationary deceleration, under this comparison basis, derives basically from the behavior of agricultural prices. The agricultural IPA reached -0.93% in March (24.70% in March 2008), while the elevation of wholesale industrial prices reached 7.22% (6.98% in March 2008). It bears noticing that, despite the effects of the exchange rate depreciation that has occurred since the third quarter of last year, wholesale industrial prices have showed deflation at the margin. As mentioned in previous Copom Minutes, the Copom evaluates that the effects of wholesale prices over consumer price inflation will depend on current and prospective demand conditions and price-setters' expectations for the future inflation path.

4. On a three-month moving average basis, according to data seasonally adjusted by the IBGE, industrial output decreased 3.3% in February, after falling by 6.3% in the previous month. Still considering the seasonally adjusted series, according to the month-to-month comparison, industrial output increased by 1.8% in February, after the 2.2% expansion observed in January. On a year-over-year basis, industrial output retreated by 17% in February, with respective falls of 18.8% and 16.9% in mining and manufacturing industries. The analysis of the behavior of IBGE industrial output series and its components, at the margin, according to data available, suggests that production would have reached its lowest level in December-January. However, the industrial activity continues to be influenced by the international crisis, due to its effects both over exports and credit conditions, and over business and households' expectations. In this context, some industrial segments have been led to adjust inventories and reduce production, a process that has recently been particularly evident in the intermediate goods industry.



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5. Among the use categories, according to data seasonally adjusted by the IBGE, the production of capital goods decreased by 6.3% in February, after increasing 4.9% in January. Regarding the other use categories, intermediate goods production increased 1.5% in February and 0.9% in January; semi-durable consumer goods production increased 1.7% in February and decreased 0.5% in January; and the production of durable goods, strongly influenced by the automotive sector increased by 10.5% in February, after a 36.2% increase in January. The recent slowdown in capital goods production reflects the persistence of the international financial turmoil and its consequences over business confidence. On its turn, the recover, at the margin, in the pace of durable goods production expansion reflects, predominantly, the exemption tax measures and also some easing of credit conditions. The future trajectory of industrial production should continue to be influenced by these factors, which counterbalance the deterioration of external demand and the process of inventories adjustment mentioned above.

6. Labor market has continued to record ambiguous indicators, combining positive aspects with signs of loss of vigor. The unemployment rate in the six metropolitan regions covered by the Monthly Labor Survey (PME) changed from 8.5% in February to 9.0% in March (8.6% in March 2008). According to the seasonally adjusted series, the unemployment rate increased 0.2 p.p., reaching 8.5%. Average real earnings increased by 4.6% in February, in year-over-year terms, and increased 5.0% in March, according to the same comparison basis, due to, in part, inflation deceleration. Employment, on its turn, expanded by 1.4% in February and 0.9% in March, in year-over-year terms. As a consequence, real payroll increased 6.6% in January and 6.2% in February, continuing to constitute a key driver for domestic demand growth. According to the National Industry Confederation (CNI) data seasonally adjusted by the BCB, manufacturing employment retreated by 0.9% in February, after decreasing by 0.8% in January and by 0.9% in December 2008. In year-over-year terms, employment declined 1.5%, and expanded by 3%, on a twelve-month trailing basis. According to data seasonally adjusted by the IBGE, manufacturing employment fell 1.3% in February (after falling 1.3% in January 2009 and 1.9% in December 2008), totaling a 1.0% increase in twelve months and a 4.2% decline year-over-year. Still regarding the labor market, data from the Ministry of Labor and Employment (MTE) indicate some recover in the generation of formal employment, despite below the seasonal pattern. In March, 34,818 jobs were created (compared to the positive result of 9,179 in February). The manufacturing industry recorded the highest dismissal rate in March, with the reduction of 35,775 jobs, followed by the commerce sector, which habitually hires in this period of the year, with the reduction of 9,697 positions. On the other hand, the civil construction sector and the services sector hired workers in the month: 16,123 and 49,280 jobs, respectively. The result for the civil construction was above the average of the last five years (13,958 jobs).

7. According to data seasonally adjusted by the IBGE, expanded retail sales increased by 2.5% in February, after increasing 5.3% in January. On a year-over-year basis, the indicator increased by 1.6%, growing by 2.2% in the year. The three-month moving average of expanded retail sales increased 2.6% in February, quarter-over-quarter, according to seasonally adjusted data, after expanding by 1.1% in January. On a month-on-month basis, according to seasonally adjusted data, it bears emphasizing the expansion in the sales of “vehicles, motorcycles, parts and pieces” (4.6%) and “other personal and domestic articles” (4.3%). The negative key drivers were “books, newspapers, magazines and stationary” (-9.1%) and “furniture and appliances” (-1.2%). In the year, cumulative growth was more significant in “office material and equipment” (13.3%) and “books, newspapers, magazines and stationary” (13.1%). After falls in October, November and December, expanded retail sales data for January and February evidence a recovery influenced mainly by the increase in the sales of vehicles, in response to the sector incentives granted by the government and some recover in the access to vehicle credit supply. For the next quarters, the retail sales trajectory will continue to be sustained by fiscal transfers, as well as by real payroll growth, whose evolution should be favored by the reduction of inflation, but it will also be affected by the evolution in the access to credit supply and by the behavior of consumer confidence.

8. The installed capacity utilization rate (Nuci) in the manufacturing industry reached 77.8% in February, below the level observed in January, according to CNI data seasonally adjusted by the BCB. According to data seasonally adjusted by CNI, the Nuci in the manufacturing industry remained stable at 77.8% in January and February. Without the seasonal adjustment, in February the Nuci stood 5.5 p.p. below the level registered in the same month of 2008. On its turn, the monthly non-seasonally adjusted Nuci calculated by Fundação Getúlio Vargas (FGV) remained stable in March at 77.0%, standing 8.2 p.p. below the level registered in the same month of 2008. The reduction in the Nuci, year-over-year, is also observed in the production of consumer goods (-5.1 p.p.), intermediate goods (-9.6 p.p.), capital goods (-15.8 p.p.) and civil construction inputs (-9.3 p.p.). The reduction on



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Nuci calculated by CNI and FGV seems to be a result of a combination between the maturity of investment projects and accommodation of economic activity, and points to significant increase of the idle capacity level of the manufacturing industry. On the other hand, data about the absorption of capital goods indicate continuity of retraction at the margin and compared to the same periods of last year. The absorption of capital goods decreased 6.7% in February, according to seasonally adjusted data, and by 25.5% in year-over-year terms, according to observed data. In its turn, the production of civil construction inputs showed stability at the margin in February, after decreasing 0.5% in January, falling 13.5% year-over-year. In short, evidences suggest an ongoing process of reduction in demand pressures over the productive capacity level of the manufacturing industry, although the speed of decline in the utilization rates has reduced. As stressed in previous Copom Minutes, the inflation trajectory is closely linked to current and prospective developments related to the expansion of supply of goods and services, to adequately meet demand conditions.

9. The twelve-month cumulative trade balance has been showing moderate growth at the margin. Under this comparison basis, the trade surplus reached US\$23.3 billion in January and increased to US\$ 24.2 billion in February and to US\$25.1 billion in March. This total resulted from US\$ 190.4 billion in exports and US\$ 165.3 billion in imports, equivalent to 15.2% and 26.0% growth, respectively, year-over-year. The adjustment in relative prices and the accommodation in the pace of expansion of domestic demand contribute to the recovery of the trade surplus, but the deterioration in the terms of trade acts on the opposite direction. The reduction in remittances of profits and dividends has contributed to limit the current account deficit, which reached US\$ 28.2 billion in December 2008, decreasing to US\$ 23.0 billion in March, equivalent to 1.6% of GDP. On its turn, foreign direct investment reached US\$41.6 billion in the twelve months through March, equivalent to 2.9% of GDP.

10. The period since the last Copom meeting was marked by the continuity of stress on international financial markets, which originated in the US and Europe, but whose impact on emerging economies has continued to be significant. However, the unprecedented actions taken by the authorities in the US and Europe, using wide range of instruments, in order to ensure minimum conditions of operation and liquidity in monetary markets, have moderated the perception of systemic risk. In this environment, there are signs, albeit incipient, of reduction in risk aversion, but the return of confidence remains fragile, due to the susceptibility of the markets to the flow of economic and non-economic news. Despite incipient, the decrease both in the risk aversion and in the scarcity of capital flows in the recent weeks encouraged the recovery of emerging economies' currencies against the US dollar.

11. Regarding the global macroeconomic scenario, contraction trends prevail over inflationary pressures. The currently predominant view points to the contraction of global economic activity in 2009, which would recover just in 2010. The consensual projections point to an intense retraction of activity in the US, Europe and Japan, which wouldn't be totally offset by the economic dynamism of some emerging economies, especially in Asia. There are evidences that the deeper weakening of economic activity in Europe and parts of Asia was in a significant manner due to the negative shock in the terms of trade caused by the elevation of commodities prices in 2008, which was reverted, allowing an increase in available income in these regions. On the other hand, the problems in the international financial system have continued to be aggravated by a cyclical deterioration in the quality of credit, focused on the US and Europe, which tends to reinforce the contraction in the financial conditions and, as a consequence, the risk of intensification in the deceleration. In mature economies, where inflation expectations are better anchored and economic activity has decelerated considerably and for a longer period, inflationary pressures have reduced rapidly. The disinflation process seems to have gained momentum also in the emerging economies, in spite of greater persistence of the inflation dynamics. In this context, monetary policies stances have become highly expansionist in the mature economies, while the expansionary stance in the emerging economies has been more moderate. At the same time, the authorities in the US, Western Europe and Asia have been announcing a series of important initiatives aimed at sustaining economic activity through fiscal incentives, which could contribute to a gradual economic recovery. It's important to notice, however, that the estimates on the fiscal costs for macroeconomic stimulus and support packages to the financial sector have been increasing, which has caused pressures over the risk assessment of several sovereign credits, even in advanced economies.

12. Oil prices remain volatile, but showed important elevation relative to the levels observed at the last Copom meeting. Future markets quotations also increased. Uncertainty concerning these quotations remains high, as the prospective scenario depends on the evolution of demand, especially in emerging economies, on the prospects for the evolution of global supply, in a scenario of uncertainty regarding the implementation and maturation of



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investments in the sector, in addition to the geopolitical issues that affect the price of this commodity. Nonetheless, despite the high uncertainty inherent to the projections regarding the trajectory of oil prices, the main scenario adopted by the Copom, which assumes unchanged gasoline prices in 2009, remains plausible, but if the current scenario in the oil market persists, it does not seem prudent to completely disregard the hypothesis of price reductions in 2009. However, it bears highlighting that, regardless of the behavior of domestic gasoline prices, the reduction in international oil prices, observed since the second half of 2008, can eventually affect domestic prices both through productive chains, such as the petrochemical, as well as through the potential effect over inflation expectations. The behavior of agricultural commodity prices, which have particularly important impact in the evolution of food costs, such as wheat, soybeans and corn, was heterogeneous since the last Copom meeting, with a predominantly upward trend, though.

### Assessment of Inflation Trends

13. The identified shocks and their impacts were reassessed according to newly available information. The scenario considered in the simulations was based in the following assumptions:

- a) similarly to the March Copom meeting, the projected adjustments for gasoline and bottled gas prices for 2009 were kept unchanged at 0%;
- b) the projected adjustments for fixed telephone for 2009 was kept unchanged at 5.0% relative to the March Copom meeting, while the expected adjustment for electricity prices was reduced to 6.3%;
- c) the projection for regulated prices inflation for 2009, based on individual items, was reduced to 5.0%, down from 5.5% considered at the March Copom meeting. This set of prices, according to data released by the IBGE, corresponded to 29.56% of the total March IPCA;
- d) the projection for regulated prices inflation for 2010 remained unchanged at 4.8%, compared to the March Copom meeting. Such projection is based on the endogenous determination model for regulated prices, which computes, among other factors, seasonal components, foreign exchange rate changes, market prices inflation and the IGP (General Price Index) variation;
- e) the projection for the spreads over the Selic rate, based on the 360-day swap rates, on the benchmark scenario, estimates a 22 bps spread in the fourth quarter of 2009 and 60 bps in the last quarter of 2010.

14. Regarding fiscal policy, the projections assume the achievement of a public sector primary surplus target of 2.5% of GDP in 2009, in comparison to 3.8% considered at the March Copom meeting. The additional assumptions considered in the previous meeting remained unchanged.

15. Since the last Copom meeting, according to the median IPCA inflation expectations compiled by the BCB's Investor Relations Office (Gerin), the 2009 IPCA reduced to 4.30%, down from 4.57%. For 2010, inflation expectations reduced to 4.30%, down from 4.50%, collected on the eve of the March Copom meeting.

16. Considering the hypotheses under the benchmark scenario – which assumes the maintenance of the exchange rate at R\$/US\$ 2.20 and the Selic rate at 11.25% p.a. during the forecast period – the projection for the 2009 IPCA decreased relative to the figure considered at the March meeting and is significantly below the 4.50% target established by the National Monetary Council (CMN). According to the forecast based on the market scenario – which incorporates the consensus exchange and Selic rates trajectories collected by Gerin on the eve of the Copom meeting – IPCA inflation forecast for 2009 also decreased compared to the figure considered in the previous Copom meeting and is also significantly below the central inflation target. Inflation projection for 2010, based on the benchmark and market scenarios, showed stability relative to the last Copom meeting. On the benchmark scenario, the projection remained significantly below the 4.5% central target, while on the market scenario it is around the central target.

### Monetary Policy Decision

17. The Copom evaluates that the monetary policy should contribute to the consolidation of a favorable long-term macroeconomic environment. Available data indicate that the pace of domestic demand expansion has significantly





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cooled since the third quarter of 2008, partially as a reaction to the substantial and generalized economic activity deceleration in other developed and emerging economies. On its turn, the increase in risk aversion and the constraint observed in liquidity conditions prevailing in the international markets observed so far, despite some marginal improvements, continue to impose adjustments in the balance of payments. Nevertheless, since the last Copom meeting, some early signs of a global risk aversion reduction, although still subject to reversion, have arisen, with impacts on both Brazilian assets and commodities, and also influencing financial conditions. However, it bears emphasizing that the trajectory of price indices, in several economies, evidences significant reduction of external inflationary pressures, especially over mature economies, but also over some emerging economies. Consequently, the net impact of the global deceleration over the domestic inflation path continues to be, until the present moment, predominantly benign. The Copom emphasizes that the main challenge of the monetary policy in such context is to ensure that the favorable results obtained over the last years are preserved.

18. The Copom evaluates that the probability that initially localized inflationary pressures may cause risk to the domestic inflation trajectory continues to diminish. Evidences of substantial accommodation of domestic demand and moderation of pressures over the market of factors, despite remaining subject to uncertainties, should reduce the risk of pass-through of upward pressures stemming from wholesale prices (which, apart from that, have showed deflation over the past few months) over consumer prices. The Committee evaluates that the materialization of such pass-through, as well as the generalization of pressures initially located over consumer prices, still depends critically on economic agents' inflation expectations. Inflation expectations for 2009 and 2010 retreated since the last Copom meeting to levels below the target, but continue to be closely monitored. Additionally, it is worth noticing that, according to available data, domestic demand behavior should exert less pressure over prices of non-tradable items, such as services, in the upcoming quarters. Anyhow, the Committee reaffirms that it will continue to conduct its actions in order to ensure that the gains obtained in inflation control in recent years become permanent.

19. The Copom emphasizes, once more, that there are important time lags between the implementation of monetary policy and its effects on economic activity and inflation. Therefore, the evaluation of alternative options for monetary policy should necessarily focus on the forward-looking inflation scenario and its risks, instead of current inflation indices. These considerations become even more relevant in periods surrounded by heightened uncertainty.

20. Prospects for the evolution of economic activity have improved since last Copom meeting, although industrial data still partially reflects an inventories' retreat process. In light of the international crisis effects over domestic financial conditions, the credit contribution to sustain domestic demand severely diminished, although there are some early signs of recovery, in particular relative to credit to individuals. The severity of the international crisis negatively influenced consumers and businessmen confidence, but there are also signs of recovery. Under such circumstances, despite some improvement on financial conditions, the resumption of economic activity will strongly depend on real payroll expansion and the effects of governmental transfers that should occur in 2009. In short, the contracting effects of the international financial crisis over the domestic economy dynamism and, consequently, over the context on which monetary policy has been acting, can become persistent, but will not be permanent. These considerations become even more relevant considering the fact that the current monetary policy decisions will have concentrated impacts in the second half of 2009 and in 2010.

21. The Copom understands that the loss of domestic demand dynamism has generated an increase in the idleness margin of factors, resulting on reduction of inflationary pressures. On the other hand, remaining risks to the inflationary dynamics derive from the trajectory of Brazilian assets prices, despite some recent recovery, associated to the partial recovery of commodities prices, amidst a process of decreasing external funding sources, as well as price adjustment mechanisms that contribute to lengthen inflationary pressures observed in the past, as evidenced by the behavior of the prices of services and regulated items since the beginning of 2009. The balance of those influences over the prospective trajectory of inflation will be crucial to the assessment of the various alternatives available for the monetary policy stance.

22. International evidence, as well as the Brazilian experience, indicates that high inflation rates leads to increase in risk premiums, both for private and public funding, to the shortening of planning horizons and, consequently, to lower potential economic growth, besides having regressive effects over income distribution. Therefore, the Copom strategy aims to ensure that inflation resumes the 4.5% midpoint target path in 2009, as established by the CMN,



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and to keep it in a level consistent with the target path for 2010. Such strategy, which should have its results evidenced throughout time, takes into account the time lags in the transmission mechanisms and is the most adequate to deal with the uncertainty inherent to the process of monetary policy formulation and implementation.

23. The Copom evaluates that, in light of signs of economic activity slowdown, regarding, for instance, industrial production indicators (which were, however, exacerbated, in some sectors, by the continuity of the inventory adjustment process), of data available for the labor market and industrial capacity utilization rates, as well as for businessmen and consumers confidence, and of lower inflation expectations for relevant horizons, the prospects for the materialization of a benign inflation scenario, in which the IPCA would resume evolution in line with the target path, have continued to increase. Indeed, the evolution of the prospective scenario is reflected on inflation projections considered by the Committee, as well as on inflation expectations set by independent analysts. The Committee also understands that the improvement on the inflation prospective scenario for 2009 and 2010 has not been, so far, incorporated into the interest rate forward structure. Nevertheless, although there is still some scope for an easing process, the monetary policy should be cautiously conducted, aiming to assure the convergence of inflation to the targets path.

24. The Committee understands that the demand slowdown, stimulated by tightening of financial conditions and by the deterioration of the agents' confidence, although some marginal improvement has been observed in both cases, as well as by the global economic activity contraction, has created a significant idleness margin of production factors that may not be rapidly eliminated in a scenario of gradual recovery of economic activity. Such development should contribute to restrain the inflationary pressures, even in light of the consequences of the adjustment process of the balance of payments and the presence of mechanisms of inflation feedback in the economy, making room for a monetary policy easing process. The Copom assessment over the scope for additional monetary easing, which depends on the inflation prospects relative to the targets path, takes into account the fact that changes on the basic interest rate have effects over activity and inflationary dynamics that accumulate over time. Additionally, the Committee understands that the continuity of the monetary easing process makes urgent the update of aspects, resulting from the long period of high inflation, still embedded within the financial system institutional framework.

25. In such context, taking into account the macroeconomic scenario and aiming to enlarge the monetary easing process, the Copom has unanimously decided to reduce the Selic rate to 10.25% p.a., without bias.

26. Under the inflation targeting regime, the Copom guides its decisions according to projected inflation, the analysis of several alternative scenarios for the evolution of the main variables that determine the forward-looking dynamics for prices, and the balance of risks associated to the projections. After a long period of expansion, domestic demand has started to exert a contractionist influence over economic activity, despite the persistence of incentive factors, such as income growth. Additionally, it bears noticing that inflation expectations for 2009 and 2010 have decreased since the last Copom meeting. On the other hand, the deceleration of global economy has generated downward pressures over wholesale industrial prices, despite the exchange rate adjustment. Under such environment, the monetary policy can be eased without jeopardizing inflation convergence to the targets path. If the risk profile deteriorates in such a manner that implies shifts to the inflation prospective basic scenario considered by the Committee at this moment, the monetary policy stance will be promptly adjusted to the circumstances.

27. At the end of the meeting, it was announced that the Committee would reconvene on June 9th, 2009, for technical presentations and on the following day, to discuss the monetary policy decision, as established in Communiqué 17.327 of August 27th, 2008.

### **SUMMARY OF DATA ANALYZED BY THE COPOM**

#### **Inflation**

28. The IPCA increased 0.20% in March, up from 0.55% in February, reaching 1.23% in the first quarter of 2009. In the last twelve months through March, the IPCA increased 5.61% compared to 5.90% in February. In March, there was deceleration on market prices (0.23%, up from 0.67% in February) and on regulated prices (0.14%, up



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from 0.28% in the previous month). In the last twelve months, market prices reached 6.44% and regulated prices increased 3.68%, compared to 6.71% and 4.02%, respectively, in February.

29. The core excluding household food items and regulated prices increased 0.25% in March, decelerating relative to the 0.88% increase observed in February, reaching 6.02% on a twelve-month trailing basis. The smoothed trimmed means core reached 0.35%, up from 0.29% in February, increasing 4.85% in the last twelve months. The non-smoothed trimmed means core reduced in March (0.21%) relative to the previous month (0.27%), reaching 4.64% in the last twelve months. The diffusion index reached 60.16%, up from 58.07% observed in February.

30. The IGP-DI decreased 0.84% in March, after a 0.13% decrease in February, reaching -0.95% in the first quarter of 2009 and 5.86% in the last twelve months. The IPA (Wholesale Price Index) decreased 1.46% in March, reflecting the reduction both in crop and livestock sector prices (2.37%) and in industrial prices (1.16%). On a twelve-month basis, the IPA increased 4.98%, with a 7.22% increase in industrial products prices and a 0.93% decrease in agricultural prices. It bears highlighting that IPA's significant deceleration in the last twelve months through September, December and March, totaling 14.33%, 9.80% and 4.98%, respectively. The IPC-Br increased 0.21% in February and 0.61% in March, reaching 6.15% and 6.32%, respectively on a twelve-month basis. The INCC recorded -0.25% in March, a record low for the series since April 1998. On a twelve-month trailing basis, the INCC reached 10.66%. IPC-Br core increased 0.39% in March, up from 0.33% in February, reaching 4.33% in the last twelve months.

31. Analyzing the IPA by stages of processing, the prices of final and intermediate goods and gross raw material reduced 0.07%, 1.84% and 2.69%, respectively, in March. In the last twelve months through March those prices increased 4.25%, 5.97% and 4.16%, respectively.

32. Partial inflation results for April indicate increase on consumer prices and a slowdown on the deceleration pace of wholesale prices, month-on-month. The IPCA-15 increased 0.36% in April, reflecting higher increases on personal expenses, housing and clothing. As for wholesale, according to the April IGP-M (Market General Price Index), there was an upturn in the prices of agricultural products, which increased in the month, and continuity of the fall in industrial prices.

### Economic Activity

33. According to seasonally adjusted data from the IBGE's monthly survey (PMC), expanded retail sales, which include construction supplies and vehicles and motorcycles, parts and pieces, increased 2.5% in February, month-on-month, reflecting the increase in the sales of seven out of the ten segments surveyed, with highlights for the performance of vehicles and motorcycles, parts and pieces (4.6%), which benefited from the IPI (Industrialized Products Tax) reduction. Sales of construction material grew 3.8% month-on-month, after four consecutive months of falling prices. Among the segments that presented decrease in sales relative to February, it bears emphasizing the negative performance of books and newspapers, magazines and stationary were highlighted, which fell 9.1%.

34. Considering comparisons between identical periods of 2009 and 2008, the increase on expanded retail sales increased 1.6% in February, growing by 2.2% in the first two months of 2009. In February, year-over-year, it bears emphasizing the performance of pharmaceuticals and medical supplies (12%); office material and equipment (11.3%); and other personal and domestic items (10.5%). The negative drivers were construction material (-12.8%); fabric, clothing and shoes (-6.9%) and furniture and home appliances (-2.1%).

35. São Paulo Trade Association (ACSP) data, related to the city of São Paulo, indicate the continuity of expansion on retail sales, with increases of 1.9% on database consultation for credit sales (SCPC) and 0.3% on consultations to the Usecheque system in March, on a month-on-month seasonally adjusted basis. Year-over-year, those indicators showed in March a 5.1% decrease and a 0.5% increase, respectively. In the first quarter of 2009 the indicators decreased 7.8% and 3.2%, respectively.

36. Automobile sales by dealers, which take into account automobiles, light commercial vehicles, trucks and buses, increased 8.3% in March, month-on-month seasonally adjusted, according to Fenabrave (Brazilian





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Federation of Auto Vehicles Distribution). On the first quarter of 2009, sales reached 668 thousand units, a 3.1% increase year-over-year, despite the 16.6% reduction on trucks sales.

37. Regarding investment indicators, capital goods production decreased 6.3% in February, month-on-month, while the production of construction typical inputs remained stable in the period, seasonally adjusted. Relative to the same period of 2008, those indicators decreased 24.4% and 13.5% in February and 19.5% and 12.3% in the first two months of 2009.

38. Capital goods imports increased 13.1% in March, month-on-month, according to the Funcex quantum indices, seasonally adjusted by the BCB. The March indicator increased 32.4% year-over-year, expanding by 4.6% in the first quarter of 2009, compared to the same period of last year, interrupting the downturn trend observed in the last months.

39. According to IBGE's Monthly Industrial Survey (PIM), industrial production increased 1.8% in February, month-on-month seasonally adjusted. Sixteen out of the 27 activities surveyed reported monthly production increase, with highlights to the performance of automobile vehicles (8.7%), other chemical products (8%), publishing and printing (10.3%) and electronic material and communication equipment (8.7%). By use categories, still considering seasonally adjusted data, it bears highlighting the increases in the production of durable consumer goods (10.5%), semi- and non-durable consumer goods (1.7%) and intermediate goods (1.5%).

40. Industrial production decreased 17% in February, year-over-year, as a reflex of a decline in all use categories: capital goods (24.4%), durable consumer goods (24.3%), intermediate goods (21%) and semi- and non-durable consumer goods (3.3%). The twelve-month cumulative industrial production declined 1% in February, compared, to the twelve months through January, when industrial production expanded by 1%, according to the same comparison basis.

41. CNI indicators showed a recovery in the industrial activity in February, month-on-month, with increases of 3.6% in real revenues and 1% in hours worked in production, according to data seasonally adjusted by the BCB. The installed capacity utilization declined 0.1 p.p. in the same period. These indicators decreased 10%, 8.3% and 5.5 p.p., respectively, year-over-year.

42. Vehicles production reached 272.4 thousand units in March, according to Anfavea, decreasing 4% year-over-year. Considering seasonally adjusted data, the production of vehicles increased 10% in March, month-on-month, for a 19.4% increase in the first quarter of this year, quarter-over-quarter. The cumulative production of vehicles decreased by 0.6% and the production of agricultural machinery increased 12.2%, in the last twelve months through March, compared to the last twelve months through February. The domestic sales of vehicles increased 8.7% in March 2009, year-over-year, accumulating a 3.9% growth in twelve months, while the exports of vehicles decreased 46.8% and 18.7%, according to the same comparison bases.

43. The LSPA survey carried out by the IBGE in March pointed to the production of 136.4 million tons in 2009, up from 135.3 million tons estimated in February. The new estimate represents a 6.5% decrease relative to the 2008 production. Declines of 12.6% and 2.3% in the production of corn and soybean, respectively, were also projected. The production of grains directly related to the basic food basket, such as rice and beans, should expand by 4.7% and 9.8%, respectively.

### **Surveys and Expectations**

44. According to the Fecomercio-SP survey, the Consumer Confidence Index (ICC) decreased 2.6% in April, month-on-month, reflecting a 4.9% reduction in the Consumer Expectations Index (IEC) and the 1.5% increase in the Current Economic Conditions Index (Icea). The ICC declined 16.2% year-over-year, mainly due to the retraction of 25.4% in the Icea.

45. According to the Consumer Expectations Survey carried out by the FGV, the ICC increased 2.5% in April, month-on-month. The confidence increase reflected the monthly increase in the components relative to consumer



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expectations (5%), whose impact in the composition of the general index overcame the effect of the 1% decline observed in the component concerning the current situation. The ICC declined 13.7% year-over-year.

46. In relation to the expectations for the manufacturing industry, the FGV Manufacturing Industry Survey showed, in March, for the third consecutive month, a slight improvement in the businessmen confidence, although the Industry Confidence Index (ICI) is at a relatively low level, when compared to the average of 2008. The ICC reached 77.9 points, after seasonal adjustment, with increase of 1.7 p.p., month-on-month, reflecting the increases of 2.2% increase in the Current Situation Index (ISA) and 2.3% in the Expectations Index (IE). According to the same survey, the installed capacity utilization (Nuci) reached 77% in March, 8.2 p.p. below the March 2008 level. Considering the seasonally adjusted series, the Nuci observed in March, 77.7%, stood 0.1 p.p. above the level registered in February.

### Labor Market

47. According to the Ministry of Labor and Employment (MTE), 34.8 thousand formal jobs were created in March after a 9.2 thousand balance in February, totaling 840 thousand jobs in twelve months. Among economic activities, services and the construction sectors registered an increase in the number of jobs in the period (49.3 thousand and 16.1 thousand, respectively), while the manufacturing industry and the retail sector recorded 35.8 thousand and 9.7 thousand dismissals, respectively. Seasonally adjusted data showed a 0.2% decline in the employment level in March, month-on-month. In the first quarter of the year, this indicator increased 3.4% influenced by increases of 8.2% in the construction sector, 4.7% in the services sector and 4.5% in the retail sector.

48. According to the IBGE employment survey (PME), carried out in the six main metropolitan areas of the country, the unemployment rate increased in March 2009 to 9%, up from 8.5% in February and 8.6% in March 2008. The monthly increase reflected the 0.7% increase in the economically active population (PEA), due to the stability in the employment level. Year-over-year, the increase in the unemployment rate was driven by the higher increase in the PEA (1.4%), relative to the 0.9% increase in the number of employed workers. The same survey pointed out that average real earnings of employed workers reached R\$ 1.321,40 in April, decreasing 0.2% month-on-month, but continued to expand significantly on a year-over-year basis (5.1%).

### Credit and Delinquency Rates

49. Outstanding credit in the financial system reached R\$1,241 billion in March, increasing by 1% in monthly terms and 25% on a twelve-month trailing basis. This volume corresponded to 42.5% of GDP, compared to December (41.3%) and March 2008 (35.5%). Non-earmarked credit operations increased 0.9% month-on-month and 23.9% in the last twelve months. Among the non-earmarked operations, which represent a share of 70.5% in the total of the financial system, credit operations to individuals increased 1.2% month-on-month and 20.9% in the last twelve months, while non-earmarked credit operations to corporate increased 0.6% and 26.7%, respectively. Earmarked credit operations increased 1.2% month-on-month and 27.5% on a twelve-month trailing basis, with highlights to the 2.5% monthly increase in housing loans.

50. Despite the 1.3% month-on-month expansion, the leasing operations in the individuals segment continue losing momentum at the margin, with a reduction of growth on a twelve-month trailing basis from 116.3% in October to 77.2% in March. Considering the segmentation by economic activity, the loans to industry increased 0.4% month-on-month and expanded 30.1% in the last twelve months.

51. The average interest rate on non-earmarked credit operations, used as reference for interest rates, reached 39.2% p.a. in March, compared to 43.3% p.a. in December and 37.6% p.a. in March 2008. The average rate on credit for individuals decreased 7.8 p.p. relative to December, reaching 50.1%. The average rate on corporate credit decreased by 1.8 p.p. relative to December, reaching 28.9%.

52. Delinquency rates in the financial system (non-earmarked loans, used as reference for interest rates, in arrears for more than ninety days) stood at 5% in March, a 0.9 p.p. increase year-over-year. Delinquency rates for credit operations with corporate and individuals reached 2.6% and 8.3%, respectively, compared to 1.8% and 6.9% in March 2008.



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53. Net delinquency rate for retail credit, measured by the ACSP, reached 9.2% in March, up from 7.6% in the same month of 2008.

### **External Environment**

54. Although many international financial market indicators have improved since the last Copom meeting, the sustainability of this movement is still uncertain. The conditions of credit markets in mature economies are still under stress, with banks limiting the access to credit. The spreads of Credit Default Swaps (CDS) of banks and corporate remain in high levels, although they have shown significant reduction in April. The final demand for goods and services, especially the one related to household consumption, signalizes stability in the US and in the Euro Area. However, the increase in the family savings continues to be the main theme in the definition of consistency and pace of consumption recovery. Private investment continues in collapse, leading to unemployment rate growth, both in mature and emerging economies. The recent estimates of the International Monetary Fund (IMF) point to 1.3% decline in global GDP in 2009 – 1.8 p.p. contraction in relation to the last January estimate -, as well as to an 11% decline in international trade in 2009.

55. Regarding inflation, the global recession outlook has contributed to disinflation and, in some cases, to deflation of energy and food prices, which has been confirmed by the disinflation trend, for example, in Canada, the Euro area and Chile, or deflationary, as observed in Swiss, Japan, China and in the US. In the US, the CPI accumulated in twelve months, pressured by the 23% reduction in energy prices, declined to -0.38% in March. In the same period, the respective CPIs indicate deflation of 1.2% in China and inflation of 0.6% in Euro area, regions where inflation reached 7.1% and 4%, respectively, in June 2008.

56. Considering the maintenance, or even a deepening, of credit restrictions, the crisis in the financial systems and the behavior of inflation, central banks from mature economies and also from emerging economies furthered the monetary policy easing. In addition to the continuous injections of capital in their local systems, the annual interest rates were lowered to 0.5%, 1.25% and 0.5% in the UK, Euro Area and Canada, respectively. The same stance was adopted, for instance, by the central banks of Chile, Turkey, New Zealand and South Africa, with interest rates at 2.25%, 9.75%, 3.0% and 9.5%, respectively. Japan and the United States continue to work with a nominal interest rate policy close to zero. It bears highlighting that in the United States, Japan and in the UK, the central banks have already started the long-run bond purchase program, aiming to facilitate the reduction of interest rates and the reduce the spread of corporate funding, which should be able to create some impulse in private investment. Additionally, in Japan, where the economic prospects have deteriorated significantly, the government, in addition to the monetary liquidity measures, announced the release of a new fiscal package totaling 15.4 trillion yens, around 3% of local GDP.

### **Foreign Trade and International Reserves**

57. The Brazilian trade surplus reached US\$1.8 billion in March, totaling US\$3 billion in the first quarter of 2009. In the month, exports reached US\$11.8 billion, and imports, US\$10 billion, decreasing by 14.9% and 21.5%, respectively, year-over-year, on a daily average basis. Total external trade recorded US\$21.8 billion in March, an 8.1% decrease year-over-year, on a daily average basis.

58. The 19.4% decline in exports in the first quarter signals the cooling of global economic activity and the effects over the prices of the main exports products. According to the Funcex indices, the prices of exports products declined 6.3% in the period, while the volume exported reduced 14.2%. In the case of Brazilian imports, the contraction of 21.6% in the same period reflected more intensely the slowdown of domestic economic activity, once the volume index decreased 20.4%, once the price index reduced 1.9%.

59. Based on the liquidity concept, international reserves, which encompass the repurchase lines and borrowing operations in foreign currencies, reached US\$ 202 billion in March, recording a US\$3.0 billion increase month-on-month. Under the cash concept, international reserves totaled US\$190 billion, recording a US\$3.5 billion increase in comparison to the end of February.



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### Money Market and Open Market Operations

60. In the period between the March and April Copom meeting, the short-term interest rates reduced significantly, influenced by the benign behavior of the current inflation indices, by the decline in inflation expectations and by the disclosure of data regarding the activity level and the labor market, considered weak. The medium- and long-term rates showed inverse movement, mainly since the beginning of April, in reaction to the investors' expectation of a faster recovery of the domestic and international economies, in response to fiscal and monetary stimuli implemented until now. Between March 9 and April 27, one-, three-, six-month and one-year rates decreased by 124 bps, 99 bps, 56 bps and 12 bps, respectively. On the other hand, the rates for two- and three-year maturity increased by 36 bps and 56 bps, respectively. Real interest rates, measured by the differential between the one-year forward nominal interest rate and the smoothed twelve-month-ahead inflation expectations, increased from 5.51% on March 9, to 5.67% on April 27.

61. In its open market operations, the BCB carried out, between March 10 and April 27, five-, six- and seven-month long fixed rate repo operations, borrowing. The six-month repo operation was carried out for the first time on April 24 and absorbed R\$ 4.0 billion. The average daily balance of these operations reached R\$41.2 billion, of which R\$25.2 billion were seven-month operations. In the same period, the BCB conducted borrowing operations with tenures of 33 and 16 working days on March 12; of 14 working days on March 23 and 30; of 12 working days on April 1; of 17 working days on April 3; of 16 working days on April 6 and of 12 working days on April 13. These operations draw from the market the following amounts: R\$203.0 billion, R\$39.0 billion, R\$5.5 billion, R\$5.0 billion, R\$8.8 billion, R\$47.9 billion, R\$0.4 billion and R\$4.0 billion respectively. The average daily balance of these short-run borrowing operations reached R\$256.6 billion. The BCB also borrowed money through 33 overnight repo operations and conducted daily, at the end of day, one- and two-working-day-tenure liquidity management operations. Operations with tenors less than thirty days, including daily liquidity management operations, averaged R\$97.6 billion, on a daily basis, borrowing.

62. On March 26, the BCB carried out traditional FX swap auctions for rolling over the contracts maturing on April 1. These operations totaled US\$4 billion, around 52% of maturing contracts. As a result, the net short position on FX swap contracts reduced from US\$ 11 billion to US\$ 7.4 billion, in notional values.

63. Between March 10 and April 27, the National Treasury issuance regarding the traditional auctions raised a total of R\$32.9 billion. The issuance of fixed-rate securities reached R\$15 billion, being R\$12.3 billion via issuance of LTNs maturing in 2009, 2010 and 2011, and R\$2.7 billion in NTN-Fs maturing in 2013 and 2017. Issuance of LFTs totaled R\$15.6 billion, for securities maturing in 2013 and 2015. Issuance of inflation-linked NTN-Bs reached R\$2.3 billion, for securities maturing in 2011, 2014, 2020, 2024, 2035 and 2045.

64. In the same period, the Treasury conducted auctions to sell LTNs maturing in October 2009 and April 2010 combined with purchases of LTNs maturing in April and July 2009, totaling R\$0.6 billion; and conducted auctions to sell LFTs maturing in September 2013, combined with the purchase of LFTs maturing in March and June 2009, totaling R\$0.3 billion. The sales of NTN-Bs settled in other National Treasury securities maturing in 2011, 2014, 2020, 2024, 2035 and 2045 totaled R\$2.0 billion. The Treasury also conducted purchase auctions of LTNs and NTN-Bs totaling R\$0.4 billion and R\$0.2 billion, respectively.