

# **Minutes of the 206<sup>th</sup> Meeting of the Monetary Policy Committee (“Copom”)\* of the Central Bank of Brazil**

April 11<sup>th</sup> and 12<sup>th</sup>, 2017



\* These minutes represent the Copom's best effort to provide an English version of the minutes of its policy meeting. In case of any inconsistency, the original version in Portuguese prevails.

**Date:** April 11<sup>th</sup> and 12<sup>th</sup>, 2017

**Place:** BCB Headquarters' meeting rooms on the 21<sup>st</sup> floor (April 11<sup>th</sup>) and 20<sup>th</sup> floor (April 12<sup>th</sup>) – Brasília – DF

**Starting and ending time:** April 11<sup>th</sup>: 10:13 am – 12:09 pm; 2:31 pm – 5:32 pm  
April 12<sup>th</sup>: 2:00 pm – 6:01 pm

**In attendance:**

**Members of the Copom**

Ilan Goldfajn – Governor  
Anthero de Moraes Meirelles  
Carlos Viana de Carvalho  
Isaac Sidney Menezes Ferreira  
Luiz Edson Feltrim  
Otávio Ribeiro Damaso  
Reinaldo Le Grazie  
Sidnei Corrêa Marques  
Tiago Couto Berriel

**Department Heads (present on April 11<sup>th</sup>)**

André Minella - Research Department (also present on April 12<sup>th</sup>)  
Ariosto Revoredo de Carvalho - Department of Foreign Reserves  
Flávio Túlio Vilela – Department of Banking Operations and Payments System  
Gilneu Francisco Astolfi Vivan – Financial System Monitoring Department  
João Barata Ribeiro Blanco Barroso – International Affairs Department  
João Henrique de Paula Freitas Simão – Open Market Operations Department  
Renato Jansson Rosek – Investor Relations and Special Studies Department  
Tulio José Lenti Maciel – Department of Economics

**Other participants (present on April 11<sup>th</sup>)**

Adalberto Felinto da Cruz Junior – Executive Secretary  
Enrico Bezerra Ximenes de Vasconcelos – Secretary to the Financial Stability Committee and Consultant to the Board  
Eugênio Pacceli Ribeiro – Head of the Deputy Governor for Economic Policy's office  
Fábio Araújo – Head of the Economic Advisory to the President  
Gustavo Paul Kurrle – Press Officer  
João André Calvino Marques Pereira – Head of the Deputy Governor for Regulation's office (present only in the morning session)  
Leonardo Martins Nogueira – Head of the Deputy Governor for Monetary Policy's office  
Luis Gustavo Mansur Siqueira – Head of the Deputy Governor for Institutional Relations and Citizenship's office (present only in the afternoon session)  
Maurício Costa de Moura – Head of the President's office  
Wagner Thomaz de Aquino Guerra Junior – Head of the Deputy Governor for International Affairs and Corporate Risk Management's office (present only in the afternoon session)

The members of the Copom analyzed the recent performance and prospects for the Brazilian and the international economies, under the monetary policy framework, whose objective is to comply with the inflation targets established by the National Monetary Council. Supplementary material to these Minutes, with economic outlook indicators, is available at the Central Bank of Brazil's webpage (<http://www.bcb.gov.br/?MINSUP2017206th>).

## A) Update of economic outlook and Copom's baseline scenario<sup>1</sup>

1. The set of indicators of economic activity released since the last Copom meeting remains consistent with stabilization of the economy in the short run. Evidence suggests a gradual recovery of economic activity during the course of 2017.

2. The economy continues to operate with a high level of economic slack, reflected in the low industrial capacity utilization indices and, mainly, in the unemployment rate.

3. The global outlook remains quite uncertain. Nevertheless, developments have so far mitigated the effects on the Brazilian economy of possible changes in economic policy in some large economies, notably in the United States. There is uncertainty regarding the sustainability of global economic growth and the stability of current commodity price levels.

4. Returning to the domestic economy, inflation dynamics remain favorable. The disinflation process has become more widespread and the disinflation of the IPCA components that are most sensitive to the business cycle and monetary policy has consolidated, increasing confidence that the ongoing disinflation process will have lasting effects. Food price disinflation constitutes a favorable supply shock.

5. Inflation expectations for 2017 collected by the Focus survey are around 4.1%. Expectations for 2018 remain around 4.5%, and expectations for 2019 and longer horizons are slightly below that level.

6. The path of administered prices, which enters the conditional forecasts for the inflation scenarios produced by the Committee, assumes increases of 6.3% for 2017, and 5.4% for 2018.

7. The scenario with interest rate and exchange rate paths extracted from the Focus survey considers, among other assumptions, exchange rates of R\$3.23/US\$ and R\$3.37/US\$ at the end of 2017 and 2018, respectively, and interest rates of 8.50% per annum (p.a.) at the end of the same periods.

8. Under these assumptions, the Committee's inflation forecast for 2017 retreated relative to the one reported in the February Copom Minutes (205<sup>th</sup>

meeting), to around 4.1%. The forecast for 2018 in this scenario remained around 4.5%.

## B) Risks around baseline inflation scenario

9. The highly uncertain global outlook might make disinflation more difficult.

10. The next steps in the process of approval of fiscal reforms involve the consideration of reforms that are fundamental to the fiscal sustainability, such as the social security reform. This process may be lengthy and involves uncertainty. These reforms and other necessary adjustments in the Brazilian economy are important for the sustainability of disinflation and for the reduction of its structural interest rate.

11. Disinflation in food prices constitutes a favorable supply shock, which might produce second-round effects, and, thus, contribute to additional reductions of inflation expectations and inflation in other sectors of the economy.

12. Economic activity points to stabilization in the short run, but its recovery might be more (or less) gradual and delayed than currently anticipated.

## C) Discussion about the conduct of monetary policy

13. The Committee members discussed the evolution of economic activity, in light of available data. They all agreed that there are signs consistent with stabilization of the economy in the short run. The prospective assessment of the Committee is that there is a small improvement in the outlook for economic recovery, compared to the Copom meeting in February (205<sup>th</sup> meeting). However, the challenges for the resumption of economic activity remain, and the Committee expects the economic recovery during the course of 2017 to be gradual.

14. Regarding the global outlook, the Committee members pointed out the uncertainties associated with possible changes in economic policy in the United States, with the sustainability of global economic growth, with the stability of current commodity price levels and also with the outlook for

<sup>1</sup> Unless explicitly stated otherwise, this update takes into account the changes that have occurred since the February Copom meeting (205<sup>th</sup> meeting).



the Chinese economy. Nevertheless, they believe that the Brazilian economy nowadays shows greater capacity to respond to occasional negative developments in the global economy, due to the progress in the disinflationary process and in the anchoring of expectations.

15. All Committee members agreed that the prospects for inflation have evolved in a favorable way since the last Copom meeting in February (205<sup>th</sup> meeting) and, to a large extent, in line with expectations. They analyzed the inflation trajectory during this and the following years. Considering the scenario that conditions on paths of the interest rate and exchange rate extracted from the Focus survey, projections for year-on-year inflation remain below the 4.5% target throughout 2017. Projections reach a trough in the third quarter of the year and increase in the last months of the year to values still below target. This difference can be partially attributed to the primary effects of the favorable food price shock. Still under the scenario with interest rate and exchange rate paths extracted from the Focus survey, the inflation trajectory reaches the 4.5% target in 2018.

16. The Copom members discussed the impacts of the revision of the tariff surcharge related to Angra III nuclear power plant over inflation in the short run. This revision may decrease April IPCA inflation by around 0.3p.p, but the return of the tariff to a level similar to the previous one should produce an opposite effect of similar magnitude in May IPCA (with residual impact in June). All members concluded that such sizable, one-off and unusual fluctuations do not have relevant implications for the conduct of monetary policy.

17. The Copom members assessed the extension of the monetary easing cycle, including its implications for the level of the policy rate throughout 2018. The extension will depend on the evolution of economic activity, on the other aforementioned risk factors, on the projections and expectations of IPCA inflation for 2018 and 2019, and also on the estimates for the structural interest rate of Brazilian economy. These estimates naturally involve uncertainty and may be reassessed by the Committee over time.

18. The Committee members reaffirmed the understanding that, with anchored inflation expectations, with inflation forecasts at the target for 2018 and a little below target for 2017, and with the high level of economic slack, the Copom's baseline scenario prescribes frontloading the monetary easing cycle.

19. Regarding the pace of monetary easing over the cycle, the Committee understands that, for a given

estimate of its extension, a possible acceleration of the pace is equivalent to greater frontloading of the cycle.

20. All members of the Copom agreed that the evolution of the economy since the February Copom meeting is compatible with the reduction of the Selic rate to 11.25 percent p.a. Everyone also agreed that this moderate intensification of the pace of monetary easing relative to the pace set in the January and February meetings is, at this time, appropriate.

21. Hence, the members of the Committee discussed the next steps for monetary policy. They emphasized, at the outset, the fundamental condition that any future decision should be compatible with the maintenance of inflation projections at the target over the relevant horizon, and with anchored inflation expectations. They also debated, on the one hand, how monetary policy could contribute to the stabilization process and subsequent resumption of economic activity and, on the other hand, the lagged effects that monetary policy could have on inflation for the coming years.

22. The Committee members pondered over the degree of frontloading of the desired cycle. On the one hand, they argued that the evolution of the economic outlook would already allow monetary easing at a faster pace than the one decided at this meeting. On the other hand, Copom members also argued that given the forward-looking nature of monetary policy, the continuity of uncertainties and risk factors that still hover over the economy would make it more appropriate to maintain the pace set at this meeting.

23. The Committee members once again emphasized that the environment with anchored inflation expectations would allow the Copom to focus on preventing second-round effects of relative price adjustments that may occur over time. This applies to the favorable food supply shock. The Copom understands that the primary effects of this supply shock, to which monetary policy should not react, should be estimated taking into account demand conditions in that sector. Monetary policy should, then, focus on possible second-round effects of this shock, which might contribute to additional reductions of inflation expectations and of inflation in other sectors of the economy.

24. All members of the Committee emphasized that the approval and implementation of reforms, notably those of a fiscal nature, and of adjustments in the Brazilian economy, including those related to credit policy and of quasi-fiscal nature, are fundamental to the sustainability of disinflation, to the full operation of monetary policy and to the

reduction of its structural interest rate, with widespread benefits for society.

25. Finally, the Committee members highlighted the importance of other reforms and investments in infrastructure aimed at increasing productivity, efficiency gains, greater flexibility of the economy, and improvement of the business environment. These efforts are fundamental for the stabilization and resumption of the economic activity and for the development of the Brazilian economy.

## **D) Monetary Policy Decision**

26. Taking into account the baseline scenario, the balance of risks, and a wide array of available information, the Copom unanimously decided to reduce the Selic rate by one percentage point, to 11.25 percent per year, without bias. This moderate intensification of the pace of monetary easing, relative to the pace set in the January and February Copom meetings, is, at this time, appropriate. The Committee judges that convergence of inflation to the 4.5% target over the relevant horizon for the conduct of monetary policy, which includes 2017 and, with a gradually increasing weight, 2018, is compatible with the ongoing monetary easing process.

27. The Copom judges that the extension of the monetary easing cycle will depend not only on estimates of the structural interest rate of the Brazilian economy, which the Committee will continue to reassess over time, but also on the evolution of economic activity, on the other aforementioned risk factors, and on inflation forecasts and expectations.

28. The Copom emphasizes that the pace of monetary easing will depend on the estimated extension of the cycle and on the degree of frontloading. In turn, the latter will depend on the evolution of economic activity, on the other aforementioned risk factors, and on inflation forecasts and expectations. The Committee considers the current pace of easing to be appropriate; however, the current economic context calls for monitoring the developments of the determinants of the degree of frontloading of the cycle.

29. The following members of the Committee voted for this decision: Ilan Goldfajn (Governor), Anthero de Moraes Meirelles, Carlos Viana de Carvalho, Isaac Sidney Menezes Ferreira, Luiz Edson Feltrim, Otávio Ribeiro Damaso, Reinaldo Le Grazie, Sidnei Corrêa Marques, and Tiago Couto Berriel.