

Inflation, measured by variations in producer price indices, pressured by rising agricultural and industrial prices, registered acceleration in the quarter ended in May, compared to the one finalized in February.

The change in consumer prices remains at a high level, despite the lesser pressure associated with the annual rise of monthly school fees and the cooling down of prices of perishable food and regulated prices. Inflation associated with market prices, highlighting in particular the pressure exerted by services, recorded acceleration at the margin, partly due to rising labor costs.

Pressures in the scope of consumer pricing should be observed in the coming months due to the pass-through of wholesale price increases. In this scenario, where twelve-month cumulative inflation rates indicate a growth tendency, there are risks of decoupling from the goal established by the National Monetary Council (CMN).

2.1 General indices

Table 2.1 – General price indices

	Monthly % change				
	2010				
	Jan	Feb	Mar	Apr	May
IGP-DI	1.01	1.09	0.63	0.72	1.57
IPA	0.96	1.38	0.52	0.68	2.06
IPC-Br	1.29	0.68	0.86	0.76	0.21
INCC	0.64	0.36	0.75	0.84	1.81

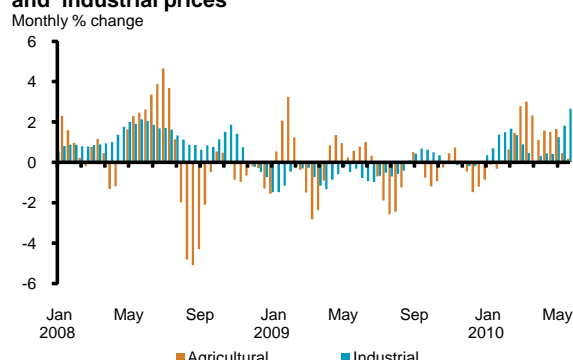
Source: FGV

The Consumer Price Index – Internal Availability (IGP-DI), published by the FGV, registered a variation of 2.95% in the quarter ended in May, up from 2.00% in the one that ended in February. The growth reflected the impact of accelerations recorded in producer prices and construction costs, the latter indicating the increase in manpower. In contrast, there was a slowdown of 0.38 p.p., to 1.84%, in the Consumer Price Index (IPC) variation. In 12-month periods, the IGP-DI posted a 4.38% growth rate in May, against 0.77% in February, the highest result in this type of comparison, since the 4.74% growth in April 2009. An upward trend in price variations of the three indicator components was registered.

The Broad Producer Price Index (IPA) grew 3.29% in the quarter ended in May, up from 2.06% in the one ended in

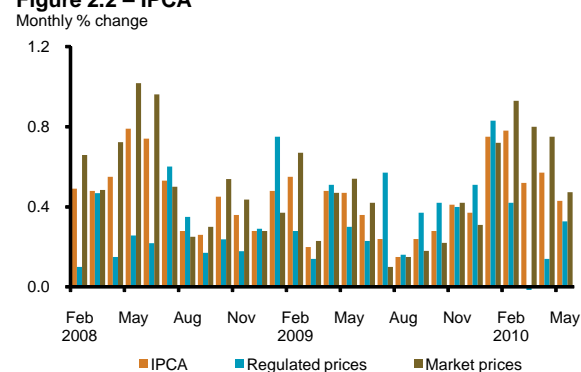
February. Agricultural prices rose 4.08% in the period, compared with a drop of 0.08% in the quarter ended in February, with emphasis on variations in beans, 67.26%; white potatoes, 39.96%; unprocessed milk, 25.52%; tomatoes, 15.81%; cotton, 11.81%; pork, 11.53%, sugarcane, 6.26%, and cattle, 6.09%. Industrial prices registered respective variations of 3.04% and 2.75% in the quarters in question, associated with acceleration, in particular, of the impact of increased prices of the metallic minerals segment, 61.16%; dairy products, 6.88%; basic metallurgy, 6.79%; and tobacco products, 5.29%, partly offset by downturns in the prices of alcohol, 26.04%, food products and beverages, 3.17%, and electronic material, a 1.75%. The cumulative IPA variation over 12 months was 3.77% in May, compared to -1.19% in February.

Figure 2.1 – IPA-10, IPA-M and IPA-DI – Agricultural and industrial prices



Source: FGV

Figure 2.2 – IPCA



Source: IBGE

Table 2.2 – Consumer prices

	Monthly % change				
	2010				
	Jan	Feb	Mar	Apr	May
IPCA	0.75	0.78	0.52	0.57	0.43
Non regulated prices	0.72	0.93	0.80	0.75	0.47
Tradables	0.68	0.26	0.53	0.61	0.42
Nontradables	0.75	1.54	1.03	0.87	0.52
Services	0.61	1.81	0.72	0.50	0.62
Regulated prices	0.83	0.42	-0.14	0.14	0.33

Sources: IBGE, Banco Central and FGV

The quarterly IPC slowdown reflected, in particular, the 0.44% falloff in Transport group prices, contrasting with the marked 5.57% expansion in the quarter ended in February. Considering 12-month periods, the indicator presented respective increases of 5.28% and 4.91% in May and February.

The National Cost of Construction Index (INCC), after registering growth of 1.10% for the quarter ended in February, increased by 3.44% in the one ended in May. This result reflected respective increases of 5.33% and 1.72% registered in the prices of labor and materials and services. Considering 12-month periods, the INCC varied 6.07% in May compared to 3.66% in February.

2.2 Consumer price indices

The IPCA, released by the IBGE, grew 1.53% in the quarter ended in May, compared to 1.91% in the one ended in February. This evolution was associated, in particular, with the slowdown of regulated prices from 1.77% to 0.32%, with emphasis on the decrease in the prices of air fares, 11.94%, and gasoline, 2.49%, which had increased 31.77% and 2.45% respectively in the quarter ended in February.

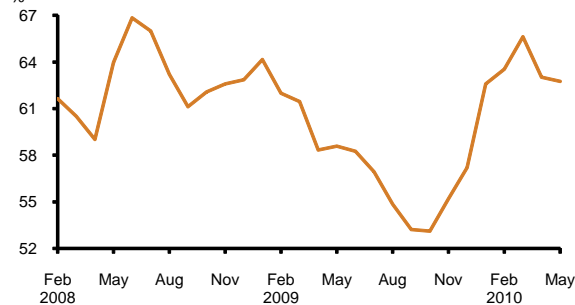
The variation in market prices reached 2.03%, compared to 1.97% in the quarter ended in February, a movement resulting from the larger impact of the 1.10% to 1.58% variation in prices of tradable goods, in relation to the reduction from 2.76% to 2.44% in those prices of non-tradable goods and services. It is worth mentioning that the quarterly performance in the prices of tradable goods reflected primarily the higher prices of beef, dairy products, apparel, and new cars.

Considering periods of 12 months, the IPCA registered a variation of 5.22% in May, up from 4.83% in February, a result of the increase from 4.77% to 5.60% in market prices, and decrease from 4.97% to 4.31% with reference to regulated prices.

The trajectory of market prices shows the recent high experienced particularly in the prices of durable and nondurable consumer goods. In this respect, the impact of increased service prices is highlighted, which, when considering a twelve-month periods, rose 6.78% in May, up from 6.23% in February, a trajectory due in large part to the accelerated prices of items domestic help and education service, which increased, respectively, by 0.84 p.p. and 1.17 p.p. over the period.

The diffusion index reached an average of 62.76% for the quarter ended in May, compared to 63.54% in the one ended in February, and 58.59% in the same period last year.

Figure 2.3 – IPCA
% of items with increase
Quarterly moving average
%



Source: IBGE

Table 2.3 – IPCA

	Weights	2010						% change
		Jan	Feb	Mar	Apr	May	Year	
IPCA	100.00	0.75	0.78	0.52	0.57	0.43	3.09	
Market prices	70.73	0.72	0.93	0.80	0.75	0.47	3.72	
Regulated prices	29.27	0.83	0.42	-0.14	0.14	0.33	1.59	
Main items								
Electricity	3.19	0.07	0.10	-0.11	-0.13	1.23	1.16	
Natural gas vehicle	0.11	-0.39	0.24	0.53	-0.39	0.57	0.56	
Pipeline gas	0.10	0.18	0.34	0.04	0.00	1.04	1.61	
Diesel fuel	0.08	0.26	0.00	-0.10	-0.30	0.03	-0.11	
Electricity	0.12	-3.83	-5.57	0.00	0.00	0.00	-9.19	
Tolls	1.30	0.00	0.00	0.31	0.00	0.00	0.31	
Water and sewage	1.61	0.00	0.00	0.74	0.08	0.84	1.67	
Urban bus	3.87	3.90	2.50	0.60	0.00	0.00	7.14	
Air ticket	0.29	-4.00	-6.57	-6.35	-5.12	-0.90	-21.02	
Gasoline	3.99	1.33	0.97	-1.95	-0.56	0.01	-0.23	
Bottled cooking gas	1.20	0.66	0.20	0.29	0.38	-0.25	1.28	
Medicine	2.84	0.06	-0.43	0.04	2.22	1.16	3.06	
Health plans	3.43	0.53	0.53	0.53	0.53	0.54	2.69	

Source: IBGE

2.3 Regulated prices

Regulated prices increased 0.32% in the quarter ended in May, contributing 0.09 p.p. to the 1.53% IPCA variation in the period. The highest pressures originated in adjustments of items medicines, 3.45%; health insurance, 1.61%; and water and sewage charges, 1.67%, the latter pressured by marked increases in Salvador, 9.29%, Goiânia, 5.29%; Brasília, 4.38%, and Belo Horizonte, 3.96%.

The cumulative change in regulated prices over 12 months reached 4.31% in May, down from 4.97% in February, while, considering the first five months of the year, there were increases of 1.58% in 2010 and 1.99% in 2009.

2.4 Inflation core

The core of the IPCA, by exclusion, registered equal variations of 0.42% in both March and April, and 0.56% in May, totaling 1.41% for the quarter that ended in May, compared to 1.74% in the one that ended in February. The indicator variation, accumulated over 12 months, reached 4.93% in May, compared to 4.86% in February.

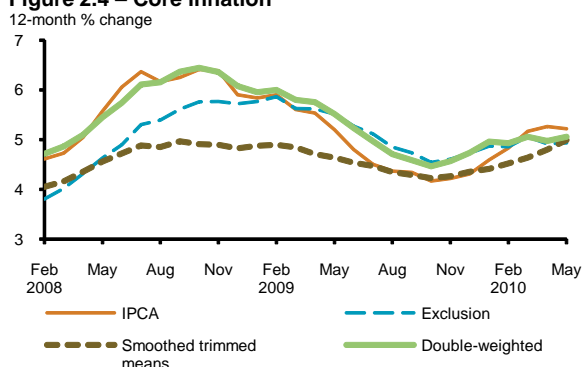
The core, calculated by smoothed trimmed-means, registered variations of 0.46% in March, 0.50% in April, and 0.62% in May, accumulating a total of 1.59% in the quarter. The

Table 2.4 – Consumer prices and core inflation

	Monthly % change				
	2010				
	Jan	Feb	Mar	Apr	May
IPCA	0.75	0.78	0.52	0.57	0.43
Exclusion	0.59	0.68	0.42	0.42	0.56
Smoothed trimmed means	0.48	0.39	0.46	0.50	0.62
Double-weighted	0.60	0.47	0.40	0.42	0.56
IPC-Br	1.29	0.68	0.86	0.76	0.21
Core IPC-Br	0.47	0.41	0.42	0.47	0.47

Sources: IBGE, Banco Central and FGV

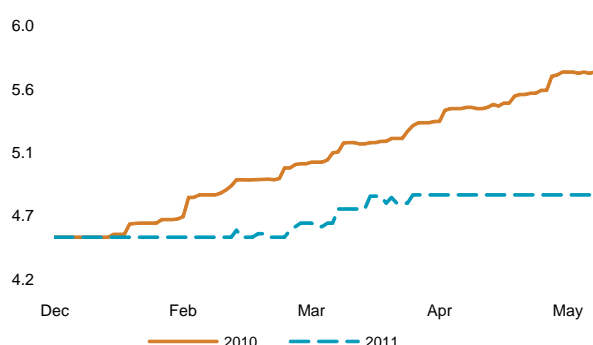
Figure 2.4 – Core inflation



Sources: IBGE and Banco Central

Figure 2.5 – IPCA

Median



criteria used to calculate this indicator excludes items in which monthly variation lies, in distribution, above the 80th percentile or below the 20th percentile, along with smoothing over twelve months the fluctuation of items whose variations are concentrated in a few periods of the year. The indicator's variation, accumulated over twelve months, was 4.99% in May, compared to 4.52% in February.

The double weighting core showed variations of 0.40% in March, 0.42% in April, and 0.56% in May, totaling 1.39% in the quarter ended in May, down from 1.55% in the quarter ended in February. Accumulated over twelve months, the indicator's variation totaled 5.06% in May, compared to 4.93% in February. This nucleus is calculated putting the original weights – based on the importance of each item to the IPCA basket – by respective degrees of relative volatility, a procedure that reduces the importance of the more volatile components.

The core inflation of the Consumer Price Index – Brazil (IPC-Br), by the FGV, calculated by the smoothed trimmed-means method, showed variations of 0.42% in March and 0.47% in April and May, totaling an increase of 1.37% in the quarter, compared to 1.21% in the one ended in February. Considering 12-month cumulative variations, the index recorded an increase of 4.16% in May, up from 3.91% in February.

2.5 Market expectations

According to the Focus Survey – Market Report from May 28, the median estimates of the annual IPCA variations for 2010 and 2011 reached 5.7% and 4.8% as compared to 4.9% and 4.5% respectively, at the end of February. The median expectation for inflation twelve months ahead – and smoothed – stood at 4.8%, compared to 4.5% at the end of February.

The medians regarding the changes in the General Price Index – Market (IGP-M) and the Producer Price Index – Domestic Supply (IPA-DI) for 2010 increased in the order of 5.9% and 5.3% at the end of February, to 8.8% and 9.5% on May 28, while those with reference to 2011 equally came to 5%, compared to 4.5% on February 26.

The median of expectations regarding growth in administered or regulated prices by contracts in 2010 has not changed since the end of February, remaining at 3.6% on May 28, while the one referring to 2011 increased from 4.5% to 4.7%.

Figure 2.6 – IGP-M and IPA-DI

Median 2010

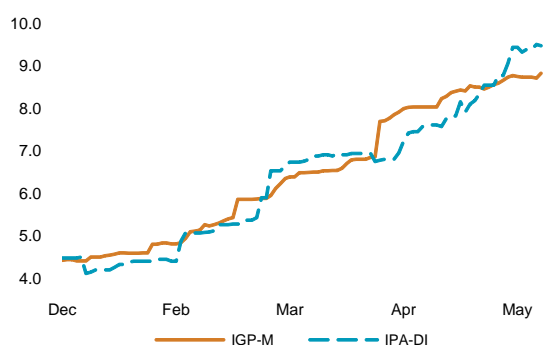
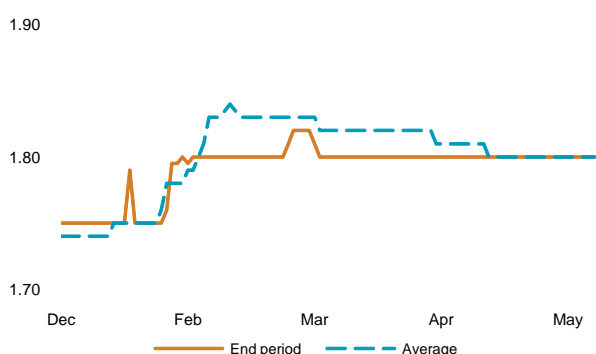


Figure 2.7 – Exchange

Median 2010



The exchange rate median projected by the market for the end of 2010 remained unchanged, at R\$1.80/US\$, while the projection for 2011 was revised from R\$1.87/ US\$ at the end of February to R\$1.85/US\$ on May 28. The median forecast for the average exchange rate regarding 2010 decreased from R\$1.83/ US\$ at the end of February, to R\$1.80/ US\$, while the median for 2011 has not changed, remaining at R\$1.84/US\$ between the 2 dates.

2.6 Conclusion

The recent evolution in consumer prices primarily reflected the depletion of seasonal pressures regarding the education group, especially the item courses, and the lesser variation of regulated prices. It is worth noting that the slowdown at the margin registered contrasts with the opposite movement in the twelve-month cumulative period, particularly with regard to the behavior of prices of tradable goods and services.

The inflation outlook in the coming months should reflect the strong performance of domestic demand, in a scenario of expanding domestic economy throughout the year, as well as likely impacts of price hikes of raw materials and labor.

Table 2.5 – Summary of market expectations

	12.31.2009		2.26.2010		5.28.2010	
	2010	2011	2010	2011	2010	2011
IPCA	4.5	4.5	4.9	4.5	5.7	4.8
IGP-M	4.4	4.5	5.9	4.5	8.8	5.0
IPA-DI	4.5	4.5	5.3	4.5	9.5	5.0
Regulated Prices	3.5	4.5	3.6	4.5	3.6	4.7
Selic (end-of-period)*	10.8	10.9	11.3	11.3	11.8	11.5
Selic (average)*	9.9	10.6	10.1	11.3	10.4	11.8
Exchange rate (end-of-period)	1.8	1.8	1.8	1.9	1.8	1.9
Exchange rate (average)	1.7	1.8	1.8	1.8	1.8	1.8
GDP growth	5.2	4.5	5.5	4.5	6.5	4.5