260th

Minutes of the Meeting of the

# Monetary Policy Committee — Copom

January 30-31, 2024

BANCO CENTRAL
DO BRASIL

**Date:** January 30-31, 2024

**Place:** BCB Headquarters' meeting rooms on the 8th floor (1/30 and 1/31 on the morning) and 20th floor (1/31 on the afternoon) – Brasilia – DF – Brazil

**Starting and ending times:** January 30: 10:06 am – 12:26 pm; 2:12 pm – 6:33 pm
January 31: 10:07 am – 11:43 am; 2:31 pm – 6:34 pm

**In attendance:**

***Copom Members***

Roberto de Oliveira Campos Neto – *Governor*
Ailton de Aquino Santos
Carolina de Assis Barros
Diogo Abry Guillen
Gabriel Muricca Galípolo
Otávio Ribeiro Damaso
Paulo Picchetti
Renato Dias de Brito Gomes
Rodrigo Alves Teixeira

***Department Heads in charge of technical presentations*** (attending on 1/30 and on the morning of 1/31):

Alan da Silva Andrade Mendes – *Department of Foreign Reserves*
André Minella – *Research Department* (also present on the afternoon of 1/31)
André de Oliveira Amante – *Open Market Operations Department*
Marcelo Antonio Thomaz de Aragão – *Department of International Affairs* (attending on 1/30)
Ricardo Sabbadini – *Department of Economics*
Rogério Antônio Lucca – *Department of Banking Operations and Payments System*

***Other participants*** (attending on 1/30 and on the morning of 1/31):

André Luiz Caccavo Miguel – *Deputy Head of the Financial System Monitoring Department*
Arnildo da Silva Correa – *Head of the Office of Economic Advisor*
Cristiano de Oliveira Lopes Cozer – *General Counsel*
Edson Broxado de França Teixeira – *Head of Office of the Deputy Governor for Supervision*
Eduardo José Araújo Lima – *Head of Office of the Deputy Governor for Economic Policy*
Euler Pereira Gonçalves de Mello – *Deputy Head of the Research Department*
Fernando Alberto G. Sampaio de Cavalcante Rocha – *Head of the Department of Statistics*
Gilneu Francisco Astolfi Vivan – *Head of the Financial System Monitoring Department*
Gustavo Andrade Barbosa de Souza – *Deputy Head of the Open Market Operations Department*
Isabela Ribeiro Damaso Maia – *Head of the Sustainability and International Portfolio Investors Unit*
Julio Cesar Costa Pinto – *Head of Office of the Deputy Governor for Monetary Policy*
Laura Soledad Cutruffo Comparini – *Deputy Head of the Department of Economics*
Leonardo Martins Nogueira – *Executive Secretary*
Luís Guilherme Siciliano Pontes – *Deputy Head of the International Reserves Department* (present on 1/30)
Mariane Santiago de Souza – *Head of the Governor's Office*
Mauro Zanatta – *Press Office Advisor*
Olavo Lins Romano Pereira – *Deputy Head of the Department of International Affairs*
Renata Modesto Barreto – *Deputy Head of the Department of Banking Operations and Payments System*
Ricardo Eyer Harris – *Head of Office of the Deputy Governor for Regulation*
Ricardo Franco Moura – *Head of the Prudential and Foreign Exchange Regulation Department*

The Copom members analyzed the recent performance and prospects for the Brazilian and international economies, under the monetary policy framework, whose objective is to achieve the inflation targets established by the National Monetary Council.

## A) Update of the economic outlook and the Copom's scenario[1]

1. The global environment remains volatile, with a debate about the beginning of the easing cycle in major economies and signs of lower core inflation, despite remaining at high levels in many countries.

2. The central banks of major economies remain committed to bringing inflation back to its targets in an environment characterized by labor market pressures. The Committee judges that the environment continues to require caution from emerging market economies.

3. Regarding the domestic outlook, the recent set of economic activity indicators remains consistent with the economic deceleration scenario expected by the Committee. Economic growth has moderated, but household consumption has been resilient. Lastly, the labor market, despite some moderation at the margin, remains strong, with acceleration of real income.

4. Consumer inflation follows the expected path of disinflation. The inflation of the components more sensitive to the economic cycle and the monetary policy are closer to the inflation target in the most recent releases. Inflation expectations for 2024 and 2025 collected by the Focus survey are around 3.8% and 3.5%, respectively.

## B) Scenarios and risk analysis

5. In the reference scenario, the interest rate path is extracted from the Focus survey and the exchange rate starts at USD/BRL 4.95[2] and evolves according to the purchasing power parity (PPP). The Committee assumes that oil prices follow approximately the futures market curve for the following six months and then start increasing 2% per year. Moreover, the energy flag is assumed to be "green" in December 2024 and 2025. In this scenario, Copom's inflation projections stand at 3.5% for 2024 and 3.2% for 2025. Inflation projections for administered prices are 4.2% for 2024 and 3.8% for 2025.

6. The Committee believes that the international environment remains volatile, marked by renewed geopolitical tensions and the debate on the beginning of the monetary policy easing in the major economies. Copom recalls that there is no mechanical relationship between the conduct of the U.S. monetary policy and the determination of the domestic policy interest rate, and that it will focus on the transmission mechanisms from the external environment to the domestic inflationary dynamics. Still on the global environment, after recognizing an improvement in the current inflation situation, the Committee focused on the sources, challenges, and uncertainties for the prospective disinflationary process. The reversal of supply shocks, the producer inflation under control in China and in the U.S., and the recent commodity price dynamics allow to extrapolate a benign scenario for goods inflation. However, great uncertainty remains about the prospective global demand and the extent of a potential residual movement in relative prices between goods and services. More recently, geopolitical tensions and the consequent rise in freight prices have added uncertainty to the prospective scenario. In addition, the dynamics of economic growth and of the labor market will be important to determine the speed of disinflation in services. These elements contribute to the debate on the nature of inflationary pressures and, potentially, on the pace of monetary easing to be adopted by advanced economies. In this context and given the recent volatility and uncertainty ahead on the international outlook, the Committee maintained its assessment that it is appropriate to adopt a cautious stance, especially in emerging countries. In addition, it will continue to monitor the data from the global economy and their respective transmission channels to the domestic economy.

[1] Unless explicitly stated otherwise, this update considers changes since the December Copom meeting (259th meeting).
[2] Corresponds to the rounded value of the average USD/BRL exchange rate observed over the ten working days ending on the last day of the week prior to the Copom meeting, according to the procedure adopted since the 258th meeting.

7. Regarding domestic economic activity, the scenario of activity slowdown anticipated by the Committee continues. However, the discussion brought elements that would allow to see a mitigation of the anticipated activity slowdown in the coming months, due to the increase in household income, as a result of the rise in the minimum wage, social benefits, and the more resilient labor market. It was mentioned that some high-frequency indicators would allow a reading that could corroborate this argument. All members, however, agreed that the Committee's reference scenario continues to be of a gradual economic growth slowdown, with resilience in household consumption and less dynamism in gross fixed capital formation. In short, activity data released since the previous meeting corroborate the scenario outlined by Copom, with no substantial change in the growth scenario.

8. Copom reinforced its view that the lack of commitment to structural reforms and fiscal discipline, the increase of earmarked credit granting, and the uncertainties about the stabilization of the public debt have the potential to raise the neutral interest rate of the economy, with harmful impacts on the power of monetary policy and, consequently, on the cost of disinflation in terms of activity.

9. The Committee noted that the labor market remains dynamic but maintained its assessment that the real income expansion may still reflect temporary issues. Copom deemed important to continue monitoring the several labor market variables very closely, in particular the dynamics of real income, which has had higher growth in recent months. The Committee also discussed more thoroughly the relationship between the labor market and prices in the economy. It highlighted the reciprocal causality between prices and the income dynamics, their respective lags, and the elasticities of impact of one on the other. Copom will continue to pay attention to the dynamics of income stemming from several surveys to better evaluate the degree of slack in the labor market and its potential impacts on the services inflation.

10. Despite the restrictive monetary conditions, Copom emphasized that the cycle of monetary easing is already being transmitted to the credit market. There are signs of increased credit granting in some lines and reduction in current interest rates on new operations, also helped by an incipient growing appetite of financial institutions to offer credit in some lines. Since the previous meeting, the capital market has shown greater dynamics.

11. On the fiscal front, the Committee reaffirms the importance of firmly pursuing the already established fiscal targets, given their importance for the anchoring of inflation expectations, and hence for the conduct of monetary policy.

12. The disinflationary dynamics did not diverge significantly from what the Committee expected, as the benign evolution of the current inflation scenario continues, and some sources that contributed to the first stage of disinflation have been exhausted. The Committee noted, however, that some aspects of recent inflationary dynamics require further investigation. It discussed, in particular, the recent dynamics of services inflation, focusing on its underlying components, and the prospective scenarios. Some members highlighted the importance of understanding the relative contributions to recent disinflation in services of the current monetary tightening and a potential spillover from disinflations in food and industrial goods. The prospective evolution of the output gap and the behavior of the labor market were again considered very relevant in determining the speed with which inflation will reach the target. A tighter labor market, with wage adjustments above the inflation target, could potentially slow down inflation convergence, notably impacting inflation in services and more labor-intensive sectors. Conversely, a favorable recovery of relative prices, a benign commodity dynamics or lower services inflation could potentially contribute to a faster disinflationary process. In its conclusion, the Committee considers that the prospective inflation scenario has not changed. Finally, the Committee has already incorporated a rise in prices due to the El Niño phenomenon into its projections and is monitoring the impacts of the phenomenon's reversal. In the end, it was unanimously concluded that a

contractionary and cautious monetary policy was needed to reinforce the disinflationary dynamics.

13. Inflation expectations remain unanchored and are a cause for concern. The Committee believes that lowering expectations requires firm action by the monetary authority, as well as continued strengthening of the credibility and reputation of both the institutions and the fiscal and monetary frameworks that make up the Brazilian economic policy.

14. The Committee emphasizes that risks to its scenarios remain in both directions. Among the upside risks for the inflationary scenario and inflation expectations, it should be emphasized (i) a greater persistence of global inflationary pressures; and (ii) a stronger-than-expected resilience of services inflation due to a tighter output gap. Among the downside risks, it should be noted (i) a greater-than-projected deceleration of global economic activity; and (ii) an impact on global inflation larger than expected from synchronized monetary policy tightening. In light of the international environment, the Committee judges that the current conjuncture remains uncertain and requires caution on the conduct of monetary policy.

## C) Discussion of the conduct of monetary policy

15. Copom then discussed the conduct of monetary policy, considering the set of projections evaluated, as well as the balance of risks for the prospective inflation.

16. The Committee believes that there has been a significant disinflationary progress, in line with what the Committee had anticipated, but there is still a long way to go to anchor expectations and return inflation to the target, which requires serenity and moderation on the conduct of monetary policy. In addition, uncertainty, particularly in this volatile international environment, recommends caution in the conduct of monetary policy. The Committee recalled that the incorporation of scenarios and exogenous variables, such as fiscal dynamics or the external scenario, takes place through their impact on the prospective dynamics of inflation, with no mechanical relationship with the determination of the interest rate.

17. The domestic scenario is moving in line with what was expected. The conclusion is that the disinflationary path of core and services inflation continues. In addition, as anticipated by the Committee, recent data suggest a moderation in economic activity. Inflation expectations for longer maturities have remained unanchored since the previous Copom meeting. Finally, inflation projections for the relevant horizon have not changed significantly, standing above the target.

18. After the scenario evaluation, all members agreed that it was appropriate to reduce the Selic rate by 0.50 percentage point to adjust the degree of prospective monetary tightening.

19. The Committee analyzed several prospective scenarios, characterized by different trajectories in the domestic and international environments. Then, it discussed the appropriate strategy and cycle length in each of these scenarios. It was decided to maintain the recent communication, which already includes the appropriate conditionality in an uncertain environment, specifying the course of action if the expected scenario is confirmed. Regarding the next steps, the Copom members unanimously anticipated cuts of 0.50 percentage point in the next meetings and judged that this pace is appropriate to keep the necessary contractionary monetary policy for the disinflationary process. This pace brings together, on the one hand, the firm commitment with the reanchoring of expectations and the disinflationary dynamics and, on the other hand, the adjustment in the level of monetary tightening in real terms in face of the more benign inflation dynamics, which was anticipated in the reference scenario projections.

20. Finally, the Committee discussed the extension of the monetary policy adjustments cycle. The Committee perceives the need to maintain a still contractionary monetary policy in the relevant horizon to consolidate the inflation convergence to the target and the anchoring of expectations. Copom emphasized again that the extension of the cycle over time will depend on the inflationary dynamics, especially the components that are more sensitive to monetary policy and economic activity, on inflation expectations, in particular the longer-term ones, on its inflation projections, on the output gap, and on the balance of risks. The Committee maintains its firm commitment to the convergence of inflation to the target in the relevant horizon and reinforces that the extension of the cycle will reflect the BCB's legal mandate.

## D) Monetary policy decision

21. Considering the evolution of the disinflationary process, the assessed scenarios, the balance of risks, and the broad array of available information, Copom decided to reduce the Selic rate by 0.50 percentage point, to 11.25% p.a., and judges that this decision is consistent with the strategy for inflation convergence to a level around its target throughout the relevant horizon for monetary policy, which includes 2024 and, to a larger degree, 2025. Without compromising its fundamental objective of ensuring price stability, this decision also implies smoothing economic fluctuations and fostering full employment.

22. The current context, characterized by a stage in which the disinflationary process tends to be slower, with only partial reanchoring of inflation expectations and a challenging global outlook, requires serenity and moderation in the conduct of monetary policy. The Committee reinforces the need to persist on a contractionary monetary policy until the disinflationary process consolidates and inflation expectations anchor around its targets.

23. If the scenario evolves as expected, the Committee members unanimously anticipate further reductions of the same magnitude in the next meetings, and judge that this pace is appropriate to keep the necessary contractionary monetary policy for the disinflationary process. The Committee emphasizes that the total magnitude of the easing cycle throughout time will depend on the inflation dynamics, especially the components that are more sensitive to monetary policy and economic activity, on inflation expectations, in particular the longer-term ones, on its inflation projections, on the output gap, and on the balance of risks.

24. The following members of the Committee voted for a reduction of 0.50 percentage point: Roberto de Oliveira Campos Neto (Governor), Ailton de Aquino Santos, Carolina de Assis Barros, Diogo Abry Guillen, Gabriel Muricca Galípolo, Otávio Ribeiro Damaso, Paulo Picchetti, Renato Dias de Brito Gomes and Rodrigo Alves Teixeira.