263rd

Minutes of the Meeting of the

Monetary Policy Committee — Copom

June 18-19, 2024

BANCO CENTRAL DO BRASIL

BANCO CENTRAL DO BRASIL

Date: June 18-19, 2024

Place: BCB Headquarters' meeting rooms on the 8th floor (6/18 and 6/19 on the morning) and 20th floor (6/19 on the afternoon) – Brasilia – DF – Brazil

Starting and ending times: June 18: 10:12 am – 11:49 am; 2:17 pm – 5:39 pm
June 19: 10:10 am – 11:25 am; 2:33 pm – 6:35 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 6/18 and on the morning of 6/19):

Alan da Silva Andrade Mendes – *Department of Foreign Reserves*
André Minella – *Research Department* (also present on the afternoon of 6/19)
André de Oliveira Amante – *Open Market Operations Department*
Marcelo Antonio Thomaz de Aragão – *Department of International Affairs*
Ricardo Sabbadini – *Department of Economics*
Rogério Antônio Lucca – *Department of Banking Operations and Payments System*

Other participants (attending on 6/18 and on the morning of 6/19):

André Maurício Trindade da Rocha – *Head of the Financial System Monitoring Department*
Aristides Andrade Cavalcante Neto – *Head of Office of the Deputy Governor for Supervision*
Arnaldo José Giongo Galvão – *Press Office Advisor*
Arnildo da Silva Correa – *Head of Office of the Economic Advisor*
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*
Fábio Martins Trajano de Arruda – *Deputy Head of the Department of Banking Operations and Payments System (present on the morning of 6/18)*
Gilneu Francisco Astolfi Vivan – *Head of the Financial System Regulation 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*
Mariane Santiago de Souza Nogueira – *Head of the Governor's Office*
Olavo Lins Romano Pereira – *Deputy Head of the Department of International Affairs*
Ricardo Eyer Harris – *Head of Office of the Deputy Governor for Regulation*
Ricardo Franco Moura – *Head of the Prudential and Foreign Exchange Regulation Department*
Simone Miranda Burello – *Advisor in the Office of the Deputy Governor for Monetary Policy* (present on the afternoon of 6/18 and on the morning of 6/19)

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 adverse because of the heightened and persistent uncertainty about the easing cycle in the United States and the speed of sustained disinflation 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 scenario, the set of indicators on economic activity and labor market continues to exhibit more strength than expected by Copom.

4. Headline consumer inflation has been following a path of disinflation, while various measures of underlying inflation are above the inflation target in recent releases. Inflation expectations for 2024 and 2025 collected by the Focus survey are around 4.0% and 3.8%, 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 5.30[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 onwards. Moreover, the energy flag is assumed to be "green" in December of years 2024 and 2025. In this scenario, Copom's inflation projections stand at 4.0% for 2024 and 3.4% for 2025. Inflation projections for administered prices are 4.4% for 2024 and 4.0% for 2025.

6. Given the more challenging scenario, the Committee analyzed and communicated an alternative scenario maintaining the interest rate constant, with a trajectory anticipated by the agents, throughout the relevant horizon. In such a scenario, inflation projections stand at 4.0% and 3.1%, respectively, for 2024 and 2025.

7. The Committee assesses that the external scenario remains adverse, due to the uncertainty regarding the U.S. interest rate cutting cycle and the persistence of the disinflation process in the main economies. More recently, some developed countries postponed the easing cycle while others opted for a cautious start to the monetary easing process. In these economies, concerns about the respective labor markets and the beginning of the easing cycle in the United States prevail. In emerging countries, however, there is greater caution due to a more challenging scenario, with the cautious continuation of interest rate cutting cycle in some countries and its interruption in others. In some emerging economies, there has been a reduction in the previously strong correlation between long-term local yield curves tenors and the U.S. Treasuries rates. In the current environment of lower liquidity, there is potentially greater differentiation among assets, relatively increasing the demand for safer assets or with better fundamentals. Copom reinforced 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, as usual, it will focus on the transmission mechanisms from the external environment to the domestic inflationary dynamics. It was also emphasized that a scenario of increased global uncertainty suggests greater caution in the conduct of domestic monetary policy, given the possibility of more abrupt movements in the prospective scenario.

[1] Unless explicitly stated otherwise, this update considers changes since the May Copom meeting (262nd meeting).
[2] Corresponds to the rounded value of the average 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.

8. Over the last quarters, economic activity data have surprised with higher growth rates in different components of demand. It was highlighted the resilience of domestic activity and the sustenance of consumption over time, in contrast to the scenario of gradual deceleration originally anticipated by the Committee. Regarding data at the margin, on the one hand, there were new upward surprises in activity. These surprises were concentrated in Gross Fixed Capital Formation and household consumption, primarily sustained by the labor market, social benefits, and court-ordered payments (*precatórios*). In turn, there is great uncertainty about the economic effects of the tragedy in Rio Grande do Sul. Uncertainties remain about the intensity of activity decline and its subsequent recovery, as well as the decrease in the stock of capital caused by the floods. Overall, the Committee assessed that the updated activity projections are in fact stronger for the year. Copom reassessed the occurrence of recurring surprises pointing to high labor market dynamics, corroborating a tight labor market scenario. The Committee believes that the output gap – which was slightly negative in the previous released assessment, but which had already been subject of analysis through different methods over the last months – is now around neutrality.

9. The Committee discussed the neutral interest rate estimates that would be used as an assumption for the projections to be analyzed. The neutral rate is an unobservable variable, subject to highly uncertainty in the estimation. There is a domestic and a global debate about the current dynamics of the neutral interest rate. In short-term changes, the emphasis is usually on productivity movements or fiscal figures, which impact domestic savings. For long-term changes, issues related to demography, productivity, and the global savings rate stand out. Due to the intrinsic uncertainty and the very nature of this variable, the Committee reinforced that the neutral rate is not a variable to be updated at a high frequency and that it is not expected to register abrupt movements either, except in exceptional cases. In this context, the Committee marginally raised the assumption for the real neutral interest rate in its models to 4.75%. Furthermore, as part of its debate, the Committee evaluated scenarios with a neutral rate between 4.5% and 5%, since many of the models presented indicate values in this range. 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.

10. The Committee closely monitors how the recent developments on the fiscal side impact monetary policy and financial assets. The Committee stresses that a credible fiscal policy, committed to debt sustainability, contributes to the anchoring of inflation expectations and to the reduction in the risk premia of financial assets, therefore impacting monetary policy. Synchronous and countercyclical monetary and fiscal policies help ensure price stability and, without prejudice to its fundamental objective, smooth out fluctuations in the economic activity level and foster full employment.

11. The Committee unanimously believes that the reanchoring of inflation expectations should be pursued, regardless of the sources behind the currently observed deanchoring, and emphasizes that the reanchoring of inflation expectations is seen as an essential element to ensure inflation convergence to the target. The Committee believes that reducing expectations requires a firm action by the monetary authority, as well as continuous strengthening of the credibility and reputation of both the institutions and the fiscal and monetary frameworks that make up the Brazilian economic policy. The Committee will not shy away from its commitment of reaching the inflation target and understands the fundamental role of expectations in the inflation dynamics.

12. Despite restrictive monetary conditions, Copom emphasized that the cycle of monetary easing is already being transmitted to the credit market, in line with what was expected. While, on the one hand, there is still historically high household

indebtedness, on the other hand, the demand for household credit remains strong. Some members emphasized, however, that the recent increase of longer-term rates could result in lower credit market dynamics. These members highlighted the importance of longer vertices in the yield curve in the determination of credit supply and demand.

13. The Committee assessed that inflation data suggested a path that did not diverge significantly from what was expected. Some members were more concerned about food inflation in the short term, highlighting not only the effect of the floods in the Rio Grande do Sul but also revisions to food prices in other regions. Services inflation continued to be a subject of much scrutiny, being analyzed through its different dimensions, lags, and prospects. Part of the debate focused on the more recent inflation path, in which industrial goods and food-at-home inflation no longer contribute to disinflation at this stage of the disinflationary process. At the same time, services inflation, which has greater inertia, plays a major role in the disinflationary dynamics at the current stage.

14. Copom concluded by assessing that the inflation outlook has become more challenging, with the increase of medium-term inflation projections, even conditioned on a higher interest rate. Benign surprises were noted in the recent period, but also the rise in projections for shorter periods, involving market prices. In the end, Copom unanimously concluded that a more contractionary and more cautious monetary policy was needed to reinforce the disinflationary dynamics.

15. 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. The Committee judges that the domestic and international environments remain more uncertain, requiring greater caution on the conduct of monetary policy. The balance of risks was again under discussion. On the one hand, it was emphasized that the reassessment of the output gap had already incorporated into the central scenario part of the upside asymmetry related to activity. On the other, there was a concern that the output gap remains resilient, and that food inflation is more persistent at the recently observed levels. After the presentation of different points of view, the Committee decided by a majority to maintain a symmetric balance of risks at this meeting.

C) Discussion of the conduct of monetary policy

16. 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.

17. The Committee unanimously decided to maintain the Selic rate at 10.50%. As far as the domestic outlook is concerned, the labor market and the economic activity, in particular household consumption, have been surprising, diverging from the expected slowdown scenario. Moreover, inflation projections for 2024 and 2025 have risen again, despite the increase in the conditioning Selic rate extracted from the Focus survey. Similarly, inflation expectations have shown additional deanchoring since the previous meeting. Moreover, the external outlook remains adverse, reflecting the market agents' view that interest rates in developed countries will remain high for a longer period.

18. Thus, the Committee considered that monetary policy should continue being contractionary for sufficient time at a level that consolidates both the disinflation process and the anchoring of expectations around the targets. The Committee will

remain vigilant and reminds, as usual, that potential future changes in the interest rate will be determined by the firm commitment of reaching the inflation target.

D) Monetary policy decision

19. Considering the evolution of the disinflationary process, the assessed scenarios, the balance of risks, and the broad array of available information, Copom decided to maintain the Selic rate at 10.50% 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 2025. Without compromising its fundamental objective of ensuring price stability, this decision also implies smoothing economic fluctuations and fostering full employment.

20. The current context, characterized by a stage in which the disinflationary process tends to be slower, further deanchoring of inflation expectations, and a challenging global outlook, requires serenity and moderation in the conduct of monetary policy.

21. The Committee unanimously decided to interrupt the easing cycle, highlighting that the uncertain global scenario and the domestic scenario, marked by resilient economic activity, an increase in its own inflation projections and deanchored expectations, require greater caution. The Committee also stresses that monetary policy should continue being contractionary for sufficient time at a level that consolidates both the disinflation process and the anchoring of expectations around the targets. The Committee will remain vigilant and reminds, as usual, that potential future changes in the interest rate will be determined by the firm commitment of reaching the inflation target.

22. The following members of the Committee voted for this decision: 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.