265th

Minutes of the Meeting of the

Monetary Policy Committee — Copom

September 17-18, 2024

BANCO CENTRAL DO BRASIL

Date: September 17-18, 2024

Place: BCB Headquarters' meeting rooms on the 8th floor – Brasilia – DF – Brazil

Starting and ending times: September 17: 10:07 AM – 12:43 PM; 2:46 PM – 6:53 PM
September 18: 10:21 AM – 11:30 AM; 2:32 PM – 6:41 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 9/17 and on the morning of 9/18):

Alan da Silva Andrade Mendes – *Department of Foreign Reserves*
André Minella – *Research Department* (also present on the afternoon of 9/18)
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 9/17 and on the morning of 9/18):

André Maurício Trindade da Rocha – *Head of the Financial System Monitoring Department*
Arnaldo José Giongo Galvão – *Press Office Advisor*
Arnildo da Silva Correa – *Head of Office of the Economic Advisor*
Cristiano de Oliveira Lopes Cozer – *General Counsel*
Daniela Torres de Mesquita de Souza Vale – *Head of the Governor's Office*
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*
Fábio Martins Trajano de Arruda – *Deputy Head of the Department of Banking Operations and Payments System (present on the morning of 9/17)*
Fernando Alberto G. Sampaio de Cavalcante Rocha – *Head of the Department of Statistics*
Fernando Ryu Ramos Kawaoka– *Deputy Head of the **Department of Economics***
Gilneu Francisco Astolfi Vivan – *Head of the Financial System Regulation Department*
Julio Cesar Costa Pinto – *Head of Office of the Deputy Governor for Monetary Policy*
Kathleen Krause – *Head of the Prudential and Foreign Exchange Regulation Department*
Leonardo Martins Nogueira – *Executive Secretary*
Luís Guilherme Siciliano Pontes – *Deputy Head of the International Reserves Department*
Olavo Lins Romano Pereira – *Deputy Head of the Department of International Affairs*
Ricardo Eyer Harris – *Head of Office of the Deputy Governor for Regulation*
Simone Miranda Burello – *Advisor in the Office of the Deputy Governor for Monetary Policy*

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 challenging, due to the inflection point of the economic cycle in the United States, which poses questions about the pace of economic deceleration, disinflation and, consequently, about the Fed's monetary policy stance.

2. The central banks of major economies remain committed to bringing inflation back to its targets in a context characterized by labor market pressures. The Committee judges that the external environment, also marked by less synchrony in monetary policy cycles across countries, continues to require caution from emerging market economies.

3. Regarding the domestic scenario, the set of indicators on economic activity and labor market has been exhibiting more strength than expected by Copom, which led to a reassessment regarding the output gap as being positive.

4. Headline inflation measured by the Extended National Consumer Price Index (IPCA) as well as 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 4.4% and 4.0%, 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 5.60[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 tariff flag is assumed to be "yellow" in December of years 2024 and 2025.

6. In the reference scenario, Copom's projections are for disinflation, but with inflation still above the target of 3.0% in the current relevant monetary policy horizon. The four-quarter inflation projection for the first quarter of 2026 is 3.5% (Table 1). Inflation projections for the calendar years 2024 and 2025 are 4.3% and 3.7%, respectively.

7. The external environment remains challenging but appears more benign than in the previous meeting. Regarding the U.S., high uncertainty persists about the degree of easing of labor market pressures and of the economic activity slowdown. It is perceived that the U.S. economy is at an inflection point, where, naturally, extracting the underlying trends of employment and activity variables is more difficult. In any case, the Committee's reference scenario is of a gradual and orderly slowdown of the U.S. economy. The Committee also discussed the Chinese slowdown and changes in commodity prices. In addition, the disinflationary process has continued in several countries, although challenges that should not be underestimated to bring inflation back to the target remain. In this regard, it was noted that, after a global inflationary shock that led to a correlated response from central banks, the specific dimensions of each economy have played a greater role, leading to a lower correlation of monetary policy cycles across countries.

8. The response of economic policies in several countries to this scenario has also been challenging. On the one hand, the Committee highlighted the role of fiscal policies as drivers of demand after the pandemic but stressed that the scope for fiscal policy has become more limited with the increase in public debt and concerns about fiscal sustainability. On the other hand, monetary policies, in such an uncertain environment, remain reactive and data-dependent in most countries, also causing inherent volatility

[1] Unless explicitly stated otherwise, this update considers changes since the July Copom meeting (264th 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.

to the markets, as observed during the recent period. Furthermore, the Committee reinforced that the central banks' commitment to achieving their targets is a fundamental ingredient in the disinflationary process, corroborated by recent indications of cautious monetary policy cycles in several countries.

9. The BRL exchange rate has shown volatility in the period, reflecting the various changes in the domestic and international scenarios. 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, nor between the exchange rate and the domestic determination of the interest rate. As usual, the Committee will focus on the transmission mechanisms from the external environment to the domestic inflation dynamics and their impact on the outlook. It was also emphasized that a context of greater global uncertainty and more abrupt exchange rate movements requires greater caution in the conduct of domestic monetary policy.

10. The Committee continues to assess that the domestic economic activity and the labor market have been more dynamic than expected, leading to a reassessment of the output gap to a positive value. Several members emphasized that the activity dynamics in the recent period has been highly relevant, highlighting the surprises for the Committee and for market analysts, as portrayed in the Focus survey. This activity growth pace, in the context of an output gap that is now considered positive, makes more challenging the process of inflation convergence to the target. The combination of a robust labor market, expansionary fiscal policy, and vigorous lending to households continue to support consumption and, consequently, aggregate demand. In a nutshell, in light of the updating of activity data for the period and of the models presented, the Committee concluded that the output gap is in positive territory.

11. The Committee noticed a persistent dynamism in the labor market, with real wage gains in recent months. As there is no evidence of a significant increase in productivity, these gains could reflect pressures on the labor market. In this regard, some members emphasized the evidence of lack of job supply in some sectors. The potential impact of the labor market on inflation was then discussed. It was argued that there is no evidence yet of wage pressures on prices, but that real wage growth, if persistent and outstripping productivity gains, will end up having an impact on prices. The Committee realizes, however, that the timing and magnitude of this transmission channel remain uncertain.

12. Copom reinforced its view that the slowdown in structural reform efforts and fiscal discipline, the increase in earmarked credit, and uncertainties over the public debt stabilization have the potential to raise the economy's neutral interest rate, with deleterious impacts on the power of monetary policy and, consequently, on the cost of disinflation in terms of activity.

13. The Committee closely monitors how the recent developments on the fiscal side impact monetary policy and financial assets. Moreover, it was noted that the market agents' more recent perception about the growth of public spending and the sustainability of the current fiscal framework, along with other factors, has had a significant impact on asset prices and expectations. A credible fiscal policy, based on predictable rules and transparency in its accounts, together with the pursuit of fiscal strategies that signal and reinforce the commitment to the fiscal framework in the coming years are important elements for anchoring inflation expectations and reducing the risk premia of financial assets, consequently impacting monetary policy. Copom incorporates in its scenarios a slowdown in the growth rate of public spending over time. 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.

14. Deanchoring inflation expectations is a factor of discomfort shared by all Committee members. Reanchoring expectations is an essential element in ensuring

that inflation converges to the target at the lowest possible cost in terms of activity. Copom believes that the conduct of monetary policy is a fundamental factor in reanchoring expectations and will continue to make decisions that safeguard credibility and reflect the fundamental role of expectations in inflation dynamics.

15. The credit cycle continues with volume expansion and interest rates reduction in most lines, both in the households and corporate segment. There is greater risk appetite in credit supply but the slight worsening in the quality of household credit has not yet become an increased materialization of risks. Capital market funding remains strong.

16. The Committee assessed that inflation data suggest a deterioration in the composition of inflation, although the aggregate index did not diverge significantly from what was expected one quarter ago. The disinflationary process was interrupted in the more recent period. Inflation rates for industrial goods and food-at-home grew at the margin, possibly reflecting the exchange rate depreciation and a more challenging climate scenario. At the same time, services inflation, which has greater inertia, plays a major role in the disinflationary dynamics at the current stage. The role of labor market dynamics and inflation expectations in determining services inflation was then discussed. The Committee concluded that current inflation, measured by the headline index or by different core measures, at levels above the target, in a context of dynamic economic activity, makes the convergence of inflation to the target more challenging.

17. Copom concluded by assessing that the inflation outlook has become more challenging, with the increase of medium-term inflation projections, even conditioned on a steeper interest rate path.

18. The Committee judges that the risks to its inflation scenarios are tilted to the upside. Among the upside risks for the inflation outlook and inflation expectations, it should be emphasized (i) a more prolonged period of deanchoring of inflation expectations; (ii) a stronger-than-expected resilience of services inflation due to a tighter output gap; and (iii) a conjunction of internal and external economic policies with an inflationary impact, for example, through a persistently more depreciated currency. 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 monetary policy tightening.

C) Discussion of the conduct of monetary policy

19. Copom then discussed the conduct of monetary policy, considering the set of projections evaluated, as well as the balance of risks for prospective inflation. The Committee focused on three dimensions in its deliberation on the monetary policy action to be taken.

20. Firstly, it assessed that the scenario, marked by resilient economic activity, labor market pressures, positive output gap, an increase in the inflation projections, and deanchored expectations, requires a more contractionary monetary policy. The Committee has outlined its response function over time, making its conduct transparent, and will pursue its mandate in full.

21. Secondly, the Committee considered that the start of the cycle should be gradual to, on the one hand, benefit from diligent data monitoring, especially in a context of uncertainties, both in external and domestic scenarios, but, on the other hand, allow the transmission mechanisms of monetary policy that will enable the convergence of inflation back to the target to begin operating. All members agreed to start the monetary policy tightening cycle gradually.

22. Thirdly, the Committee discussed the pace and magnitude of the interest rate

adjustment, as well as its communication. In view of the uncertainties involved, the Committee preferred a communication that reinforced the importance of monitoring the scenarios over time, without giving any future indication of its next steps but insisting on its firm commitment to the convergence of inflation to the target.

D) Monetary policy decision

23. The scenario, marked by resilient economic activity, labor market pressures, positive output gap, an increase in the inflation projections, and deanchored expectations, requires a more contractionary monetary policy. Considering the evolution of the disinflationary process, the assessed scenarios, the balance of risks, and the broad array of available information, Copom unanimously decided to increase the Selic rate by 0.25 p.p. to 10.75% 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. Without compromising its fundamental objective of ensuring price stability, this decision also implies smoothing economic fluctuations and fostering full employment.

24. The pace of future adjustments of the interest rate and the total magnitude of the cycle that has just started will be determined by the firm commitment of reaching the inflation target and will depend on the inflation dynamics, especially the components that are more sensitive to monetary policy and economic activity, on the inflation expectations, on the inflation projections, on the output gap, and on the balance of risks.

25. 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.

Table 1

Inflation projections in the reference scenario

Year-over-year IPCA change (%)

Price index	2024	2025	2026Q1
IPCA	4.3	3.7	3.5
IPCA market prices	4.4	3.6	3.4
IPCA administered prices	4.2	4.0	3.9