

## Brazil | BCB is concerned with the impact of fiscal uncertainty and "non-economic events"

Enestor Dos Santos

---

The BCB sees 2016 inflation at 6.2%/6.3%, in line with its goal for the period. Moreover, it forecasts 2017 inflation to reach 4.8%/4.9%, which we see as sufficiently close to the 4.5% level it wants to make inflation to converge to. If our view is correct, and if fiscal uncertainty and "non-economic events" allow it, the Selic rate will be left unchanged in January.

### The hawkish tone employed in the previous monetary policy minutes was broadly preserved in the 4Q15 Inflation Report

The wording and the tone of today's report was similar to the one used in [the minutes of the last monetary policy meeting at the end of November](#). The concerns about the impact on inflation of fiscal deterioration were highlighted again. The recent worsening in inflation expectations were explicitly attributed to the "increase in the uncertainties related to the fiscal results". Together with the effects of the realignment of regulated prices and the exchange rate depreciation, fiscal deterioration was presented as the responsible for inflation actually being at very high levels. However, differently from the [most recent monetary policy minutes](#), this time the BCB also underscored that uncertainties related to the development of "non-economic events [an implicit reference to the ongoing political turmoil] influence and will continue to influence, if not timely addressed, the prices of financial assets".

### Monetary policy goals were made explicit, revealing more tolerance with inflation in 2016

As previously, the BCB affirmed that "monetary policy should remain especially vigilant to make sure that short-term [inflationary] pressure do not propagate into longer horizons" and that it "shall take the necessary measures to ensure the fulfillment of the inflation targets". Regarding the latter, the monetary authority explicitly stated its goals as "circumscribe inflation within the limits established by the CMN [the National Monetary Council], in 2016, and make it to converge to the 4.5% target, in 2017". The goal of taking inflation as close as possible to 4.5%, presented in [the last monetary policy minutes](#), was not included in the 4Q15 Inflation Report, showing some higher degree of tolerance with inflation next year.

### The BCB inflation forecasts are already broadly in line its goals

Today's report showed that the BCB expects inflation to converge to 6.2%/6.3% in 2016 and to 4.8%/4.9% in 2017. Its forecasts for 2016 are already in line with its goal for the period (i.e. to take inflation within the 2.5%-6.5% target range). To some extent, the slowdown of inflation from around 10.8% in 2015 is due to the sharp expected contraction in domestic demand (the BCB expects GDP to contract by 3.6% in 2015 and by 1.9% in 2016). Regarding 2017, we see BCB forecasts as sufficiently close to its 4.5% target for the period. If our view is correct, no further monetary tightening would be needed for the BCB to meet its goals and, therefore, the Selic rate would be left unchanged at 14.25% in the next monetary policy meeting in January. However, if our view is not shared by the BCB (i.e. if it regards its 4.8%/4.9% inflation forecast for 2017 significantly higher than its 4.5% target) or if the concerns about fiscal deterioration and the political environment gain momentum, the Selic rate could then be adjusted upwards.



This document has been prepared by BBVA Research Department, it is provided for information purposes only and expresses data, opinions or estimations regarding the date of issue of the report, prepared by BBVA or obtained from or based on sources we consider to be reliable, and have not been independently verified by BBVA. Therefore, BBVA offers no warranty, either express or implicit, regarding its accuracy, integrity or correctness.

Estimations this document may contain have been undertaken according to generally accepted methodologies and should be considered as forecasts or projections. Results obtained in the past, either positive or negative, are no guarantee of future performance. This document and its contents are subject to changes without prior notice depending on variables such as the economic context or market fluctuations. BBVA is not responsible for updating these contents or for giving notice of such changes.

BBVA accepts no liability for any loss, direct or indirect, that may result from the use of this document or its contents.

This document and its contents do not constitute an offer, invitation or solicitation to purchase, divest or enter into any interest in financial assets or instruments. Neither shall this document nor its contents form the basis of any contract, commitment or decision of any kind.

In regard to investment in financial assets related to economic variables this document may cover, readers should be aware that under no circumstances should they base their investment decisions in the information contained in this document. Those persons or entities offering investment products to these potential investors are legally required to provide the information needed for them to take an appropriate investment decision.

The content of this document is protected by intellectual property laws. It is forbidden its reproduction, transformation, distribution, public communication, making available, extraction, reuse, forwarding or use of any nature by any means or process, except in cases where it is legally permitted or expressly authorized by BBVA.