XVI Monetary Policy Managers Meeting
CEMLA and Banco de la República

Monetary Policy in Brazil
in Extraordinary Times

André Minella
Research Department
September 13 and 14, 2021
Brazilian economy before the pandemic

- Gradual recovery underway
- Actual and projected inflation around the target
- Monetary policy easing: Policy rate (Selic) at the lowest historical level: 4.25% p.a.

<table>
<thead>
<tr>
<th>Inflation: BCB's projections and professionals' forecasts before the pandemic</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td>Target</td>
</tr>
<tr>
<td>BCB's projections**</td>
</tr>
<tr>
<td>Focus Survey***</td>
</tr>
</tbody>
</table>

* Actual values
** Copom Meeting on Feb 4-5, 2020. Scenario with interest rate path extracted from the Focus survey and constant exchange rate.

Source: IBGE; BCB.
Pandemic hit hard the Brazilian economy

- GDP fell by 11.1% in 2020Q2 vis-à-vis 2019Q4
- CPI decreased by 0.69% in Apr-May 2020
- Economic uncertainty skyrocketed
Policy responses

- Combination of policies and measures

**Central Bank of Brazil**
- Monetary and FX policies
- Liquidity and Capital

**Ministry of Finance**
- Credit measures
- Direct transfers
- Tax reliefs and deferrals
Monetary policy in unknown territory

- Inflation projections and expectations fell significantly to below-target levels
- Selic rate reached 2.00% p.a. in August (-50, -75, -75, -25 bp) from 4.25% p.a. in February
- Historical lows: level and differential with the U.S.

Note: Focus Survey is conducted among professional forecasters. Last data point: Dec. 31, 2020. Source: BCB (Focus Survey).
Liquidity and credit support measures

- EMEs – Comparative overview of announced measures
Credit market

- Policies were effective in the credit market, both in rates and volumes
- Credit to corporates increased significantly
- Credit to household fell, but much reflecting reduction in demand
Countercyclical fiscal policy

- Emergency Transfer Programs
- Deferral of tax payments

Discretionary fiscal response to the COVID-19 crisis in selected economies (% of GDP)

Public debt has increased, although less than expected

- Gross-government-debt-to-GDP ratio went to 88.8% in 2020 from 74.3% in 2019
- Consensus forecasts peaked at 94.6%
Vaccination has accelerated

- Pandemic has receded significantly recently
- Most of adult population has received at least one dose

Note: Last data point: September 8, 2021.
Source: Our World in Data.

Note: Last data point: September 8, 2021.
Source: Ministry of Health.
Brazilian economic recovery

• V-Shaped recovery: GDP at the same level as the pre-pandemic level
• Labor market recovering, but its strength with mixed signals
Inflation pressures

- Inflation pressures higher than in the pre-pandemic period
- Economic recovery + commodity prices + bottlenecks + energy crisis

Source: IBGE; BCB.

### Inflation: Selected items - Aug/2021 (yoy) %

<table>
<thead>
<tr>
<th>Category</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gasoline</td>
<td>39.09</td>
</tr>
<tr>
<td>Bottled gas</td>
<td>31.07</td>
</tr>
<tr>
<td>Electricity</td>
<td>21.08</td>
</tr>
</tbody>
</table>

Source: IBGE; BCB.
Surge in commodity prices without exchange rate relief

- Commodity prices in domestic currency 50%-60% higher than in the pre-pandemic period
- Historically inverse relationship between terms of trade and the value of domestic currency

---

**Note:**
- CRY – US$, CRY – R$ (Jan 1, 2019 = 100)
- Source: Bloomberg; BCB

**Terms of trade and real effective exchange rate**

(indexes, Jan/03 = 100)

**Note:**
- CRY – US$, CRY – R$ (Jan 1, 2019 = 100)
- Source: Secex; BCB
Sectoral bottlenecks and energy crisis

• Some sectors facing shortage of raw materials, affecting the production
• Drought leading to energy crisis, resulting in substantial increase in electricity prices

Source: FGV.

Stored energy
(southeast/midwest hydroelectric subsystem)

Source: ONS.
Rise in inflation projections and agents’ expectations

- Above the upper limit of the tolerance interval for 2021

Note: Focus Survey is conducted among professional forecasters. Last data point: Sept. 3, 2021. Source: BCB (Focus Survey).
Rise in the policy rate: actual and expected

- End of the extraordinary degree of monetary stimulus
- BCB started raising the Selic rate in March from the low of 2.00%, currently at 5.25%
- The strategy of a quicker monetary adjustment is the most appropriate to guarantee the anchoring of inflation expectations.

Selic rate trajectory expectations - Focus Survey

Selic real rate - Focus Survey
(four-quarter ahead)

Note: Selic real rate calculated as the four-quarter-ahead nominal Selic rate, discounted from inflation expectations for the same period, both variables extracted from the Focus Survey. Source: BCB (Focus Survey).
Final remarks

• Pandemic hit hard the Brazilian economy, but response was strong, involving a combination of monetary, fiscal, credit, FX, liquidity and capital measures.

• Economic activity has rebounded, although labor market with mixed signals about its recovery’s strength

• Inflationary pressures coming from the economic recovery, surge in commodity prices, global bottlenecks, and energy crisis

• Monetary policy response to curb inflation pressures and tame inflation expectations