

# 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.

Inflation: BCB's projections and professionals' forecasts before the pandemic

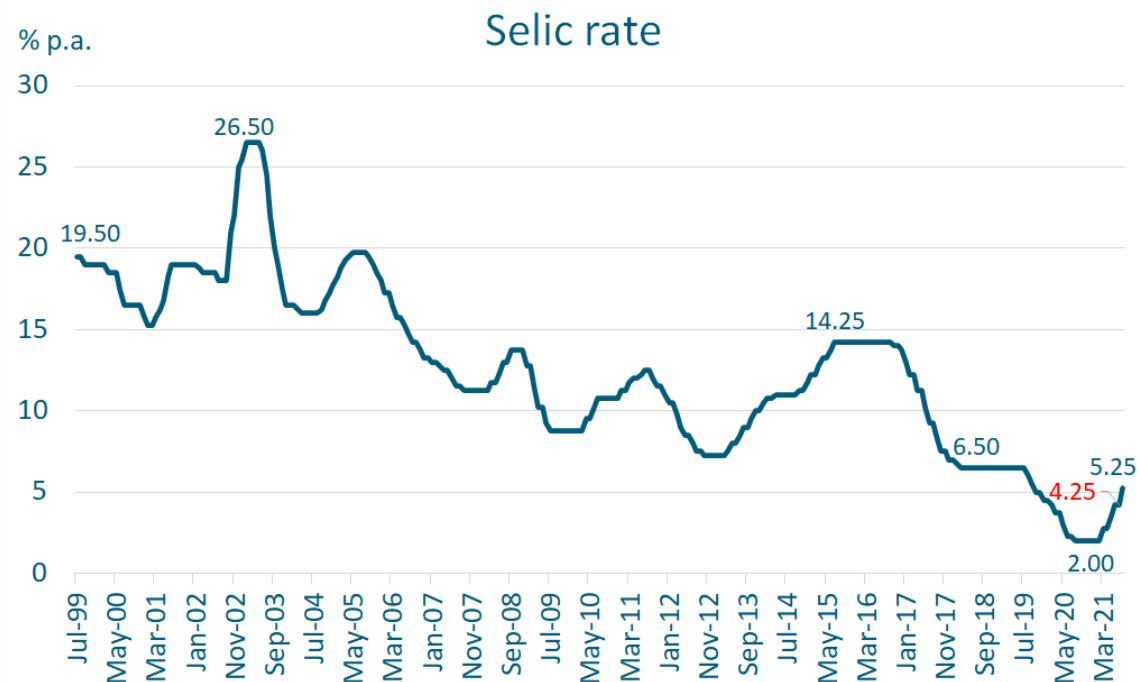
	2019*	2020	2021
Target	4.25	4.00	3.75
BCB's projections**	4.31	3.5	3.7
Focus Survey***	4.31	3.40	3.75

\* Actual values

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

\*\*\* Survey conducted among professional forecasters on Jan 30, 2020.

Source: IBGE; BCB.



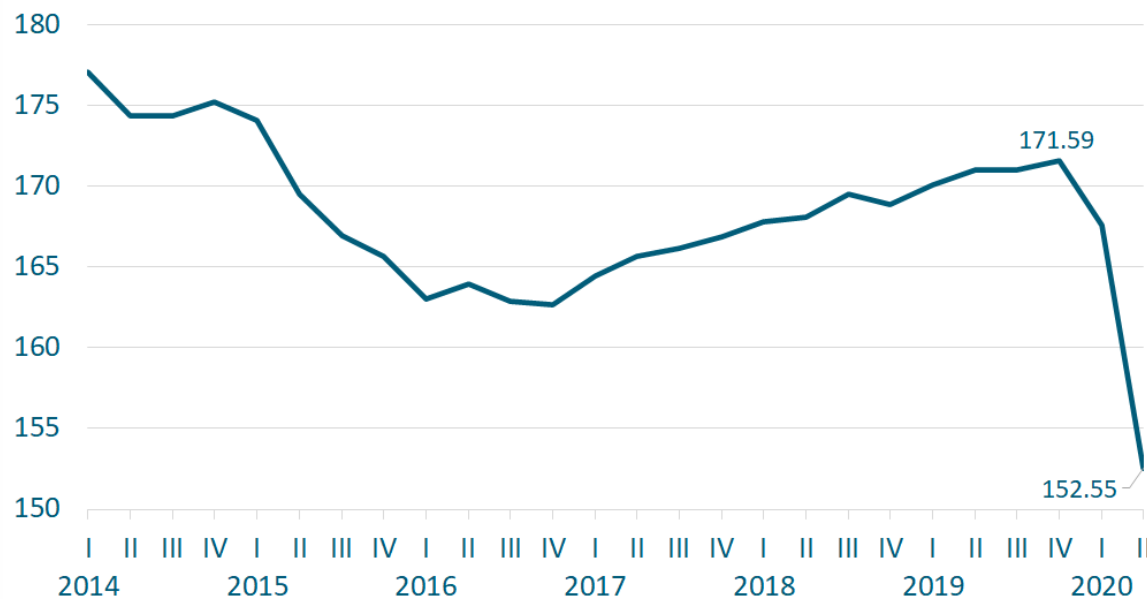
Note: Selic target at the end of each month.

Source: BCB.

# Pandemic hit hard the Brazilian economy

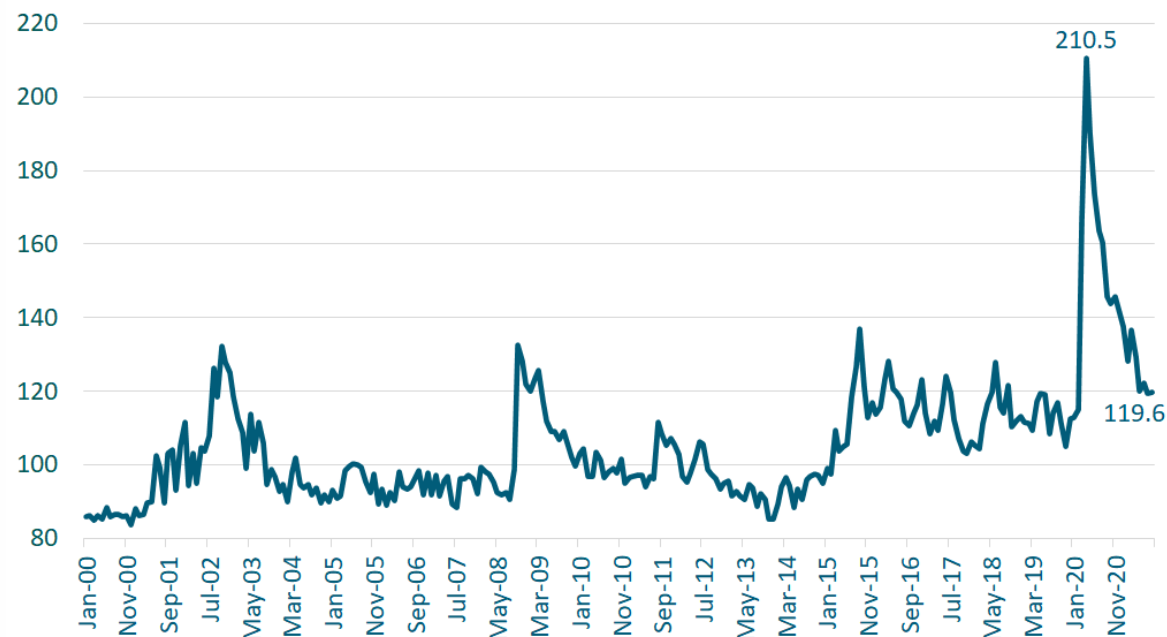
- GDP fell by 11.1% in 2020Q2 vis-à-vis 2019Q4
- CPI decreased by 0.69% in Apr-May 2020
- Economic uncertainty skyrocketed

GDP index  
(seasonally adjusted)



Source: IBGE.

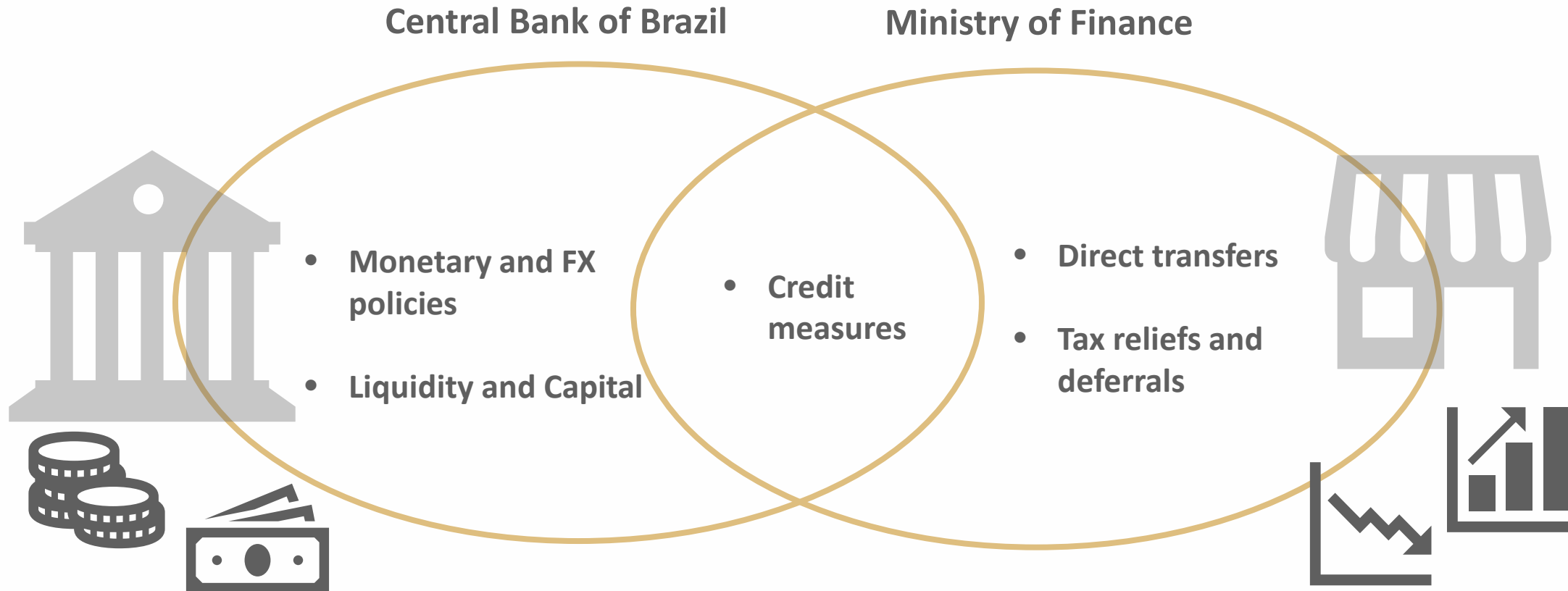
Economic Uncertainty Indicator - Brazil (IIE-Br)



Source: FGV.

# Policy responses

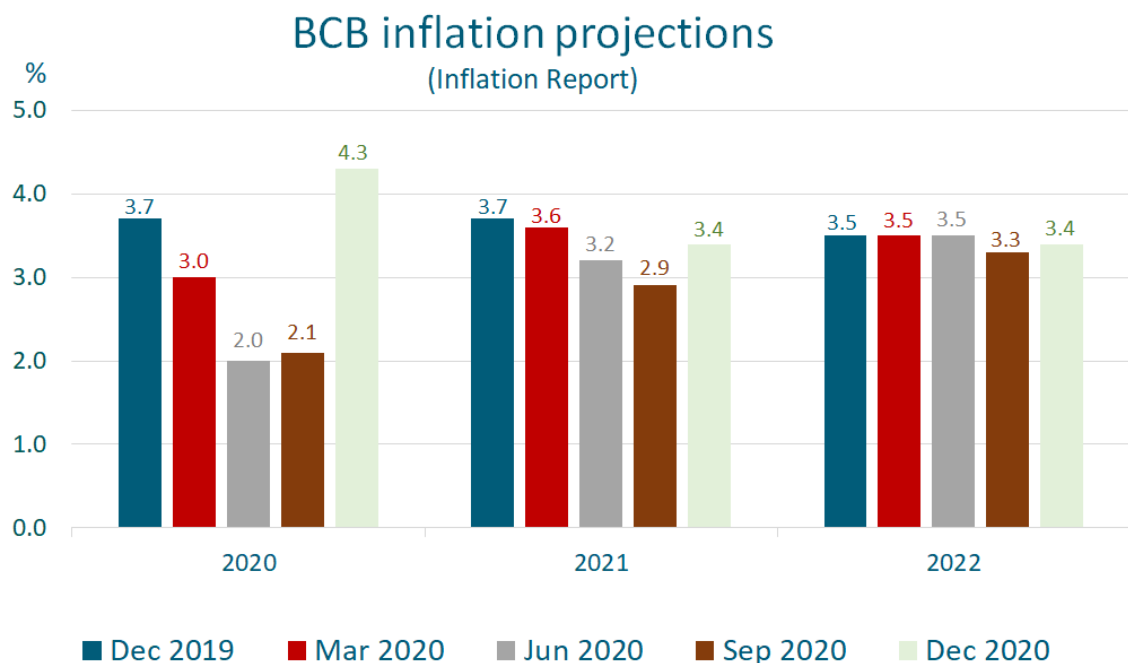
- Combination of policies and measures



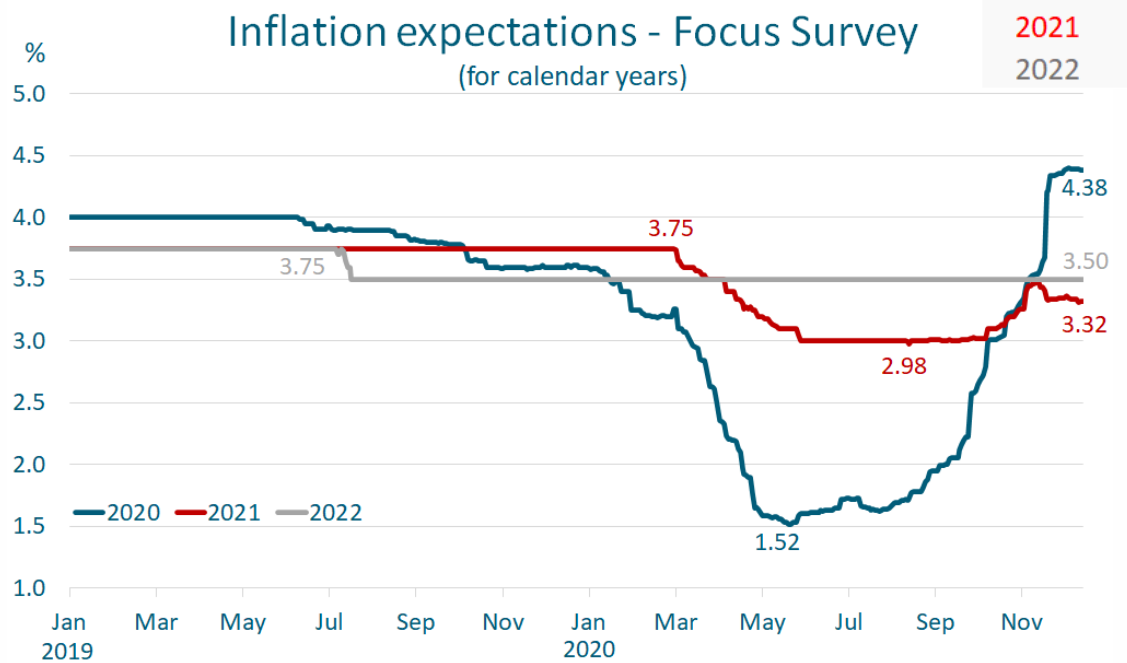
# Monetary policy in unknown territory

- 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.

Inflation target	
2020	4.00
2021	3.75
2022	3.50



Source: BCB.

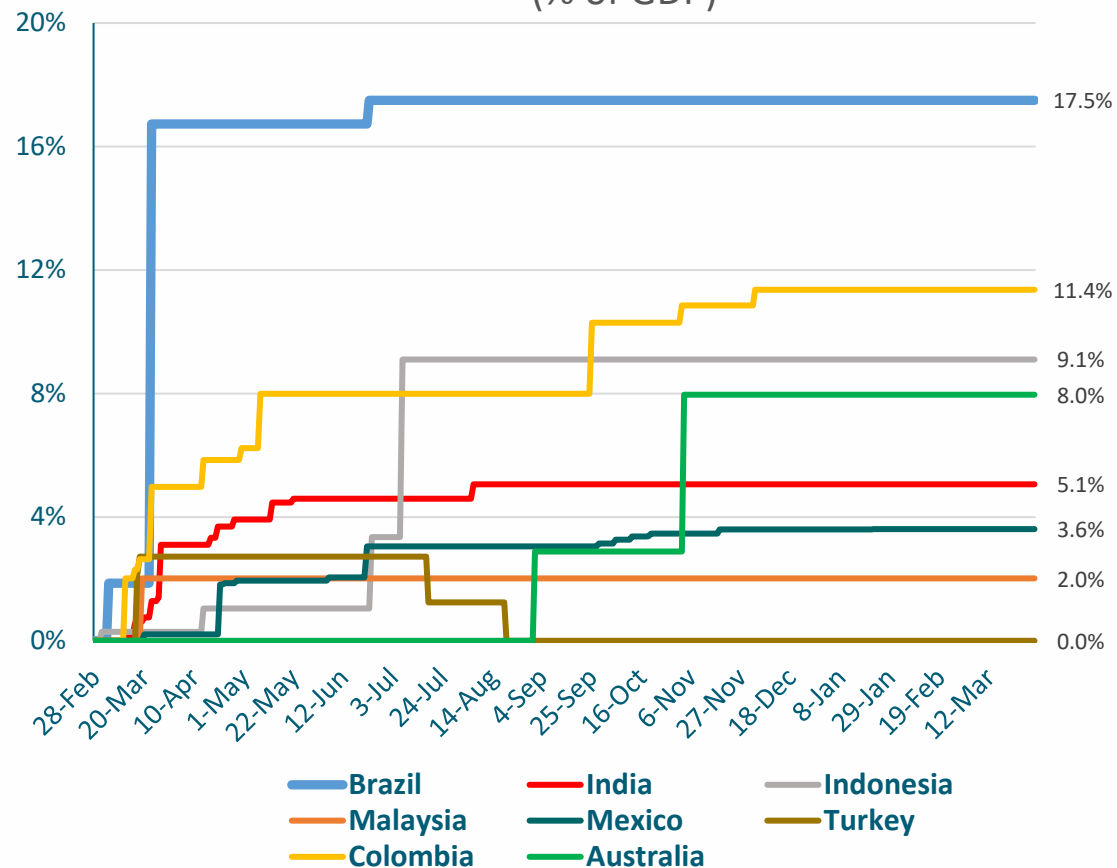


Note: Focus Survey is conducted among professional forecasters. Last data point: Dec. 31, 2020.  
Source: BCB (Focus Survey).

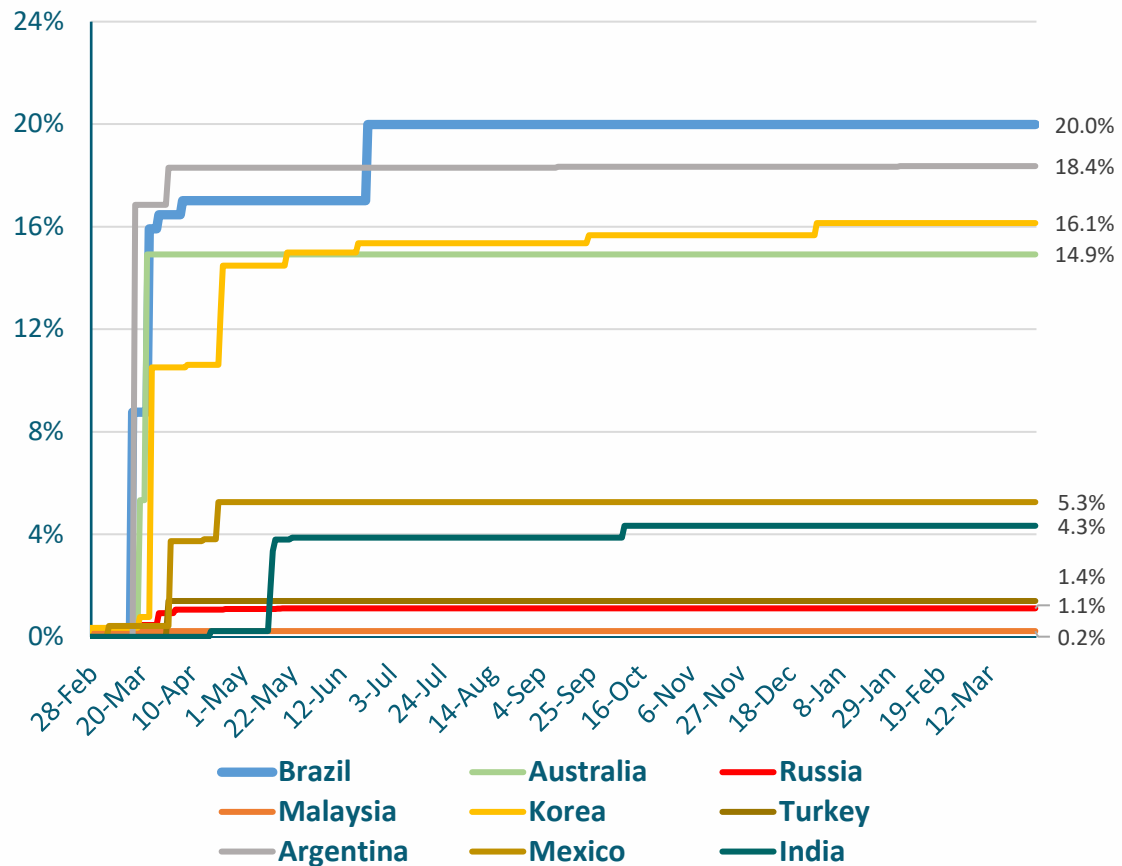
# Liquidity and credit support measures

- EMEs – Comparative overview of announced measures

**Liquidity Support**  
(% of GDP)



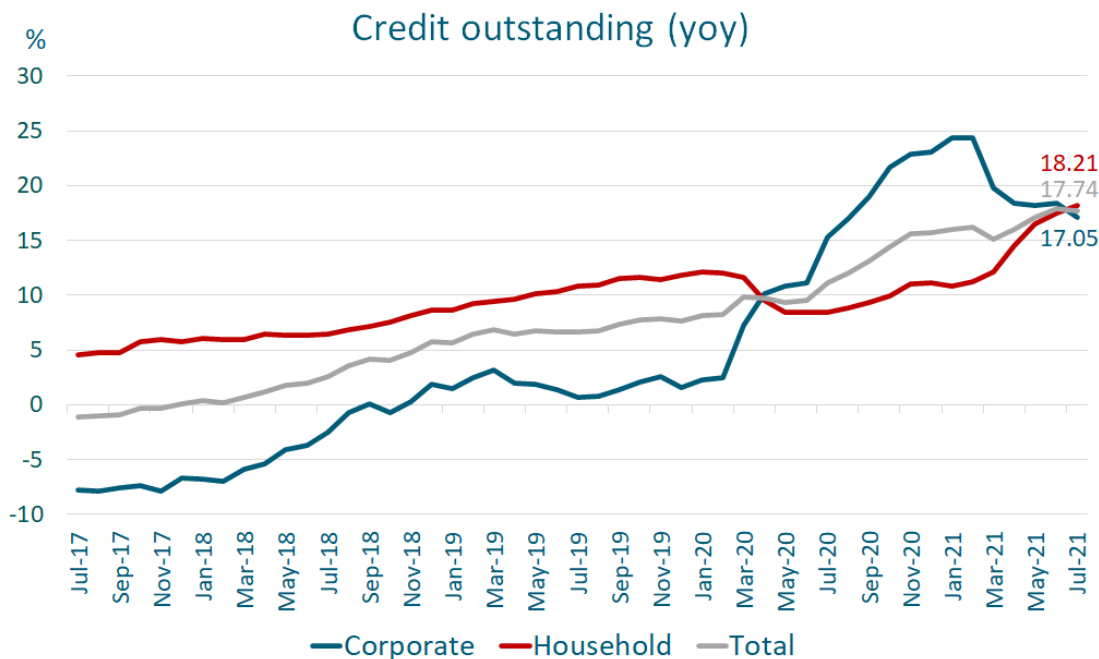
**Credit Support**  
(% of GDP)



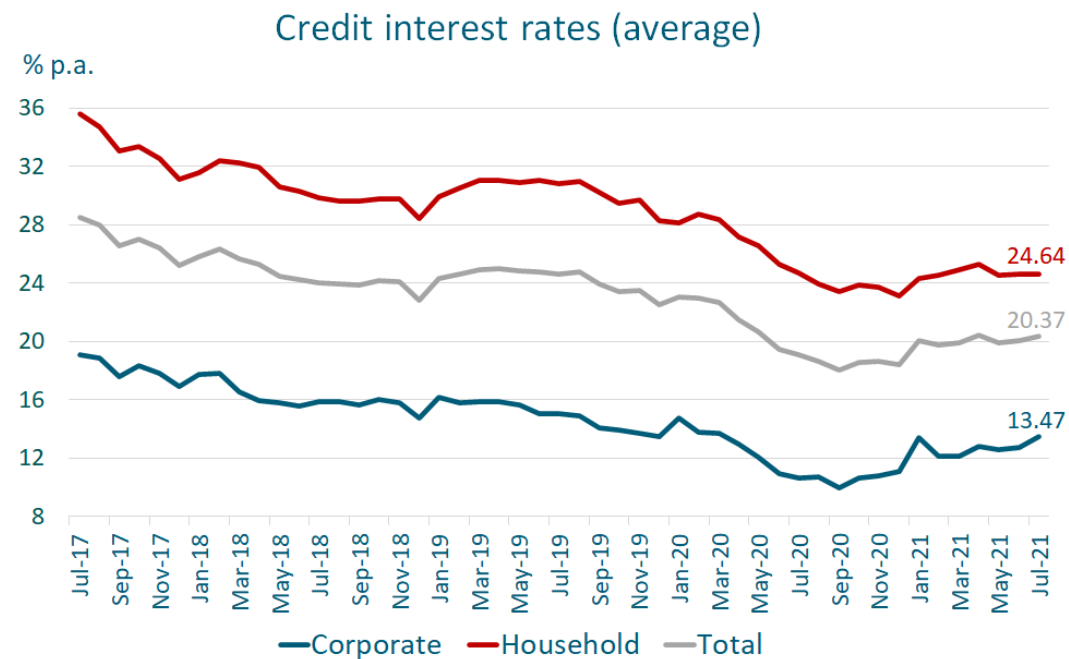
Source: FSB/BCB

# 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



Source: BCB.

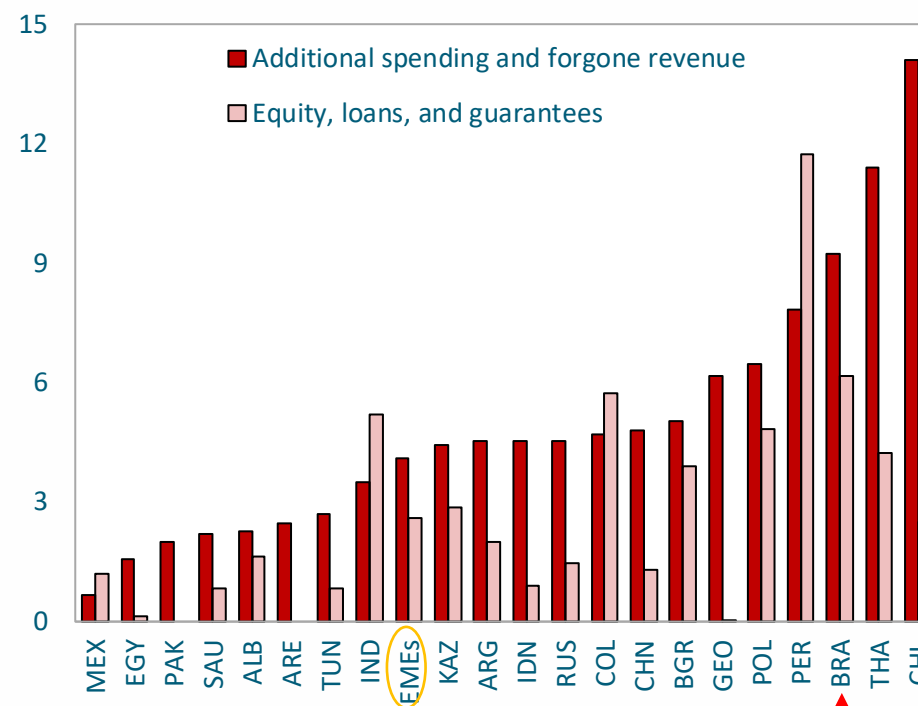
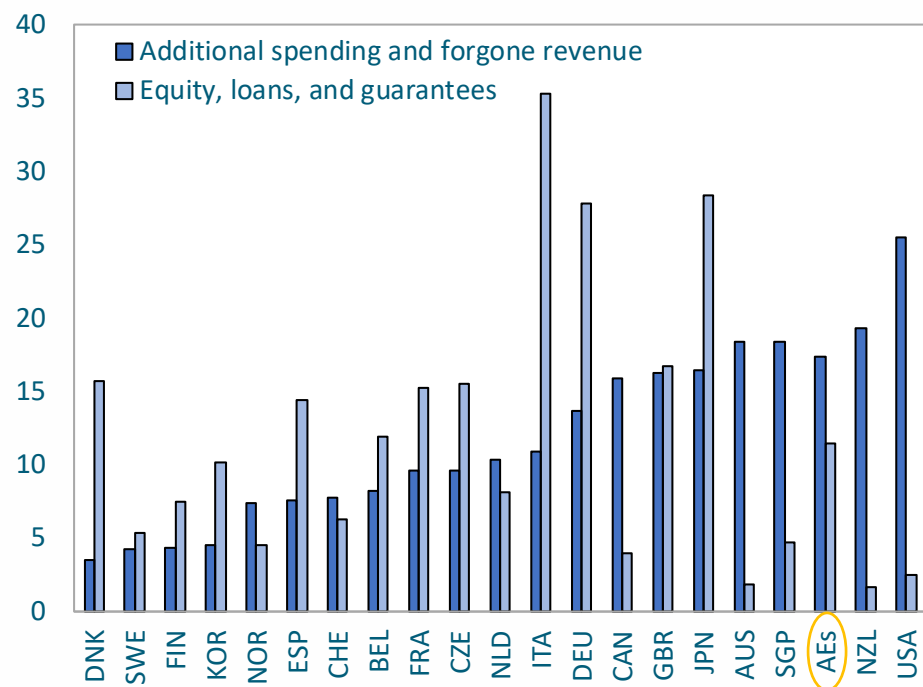


Source: BCB.

# Countercyclical fiscal policy

- Emergency Transfer Programs
- Deferral of tax payments

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



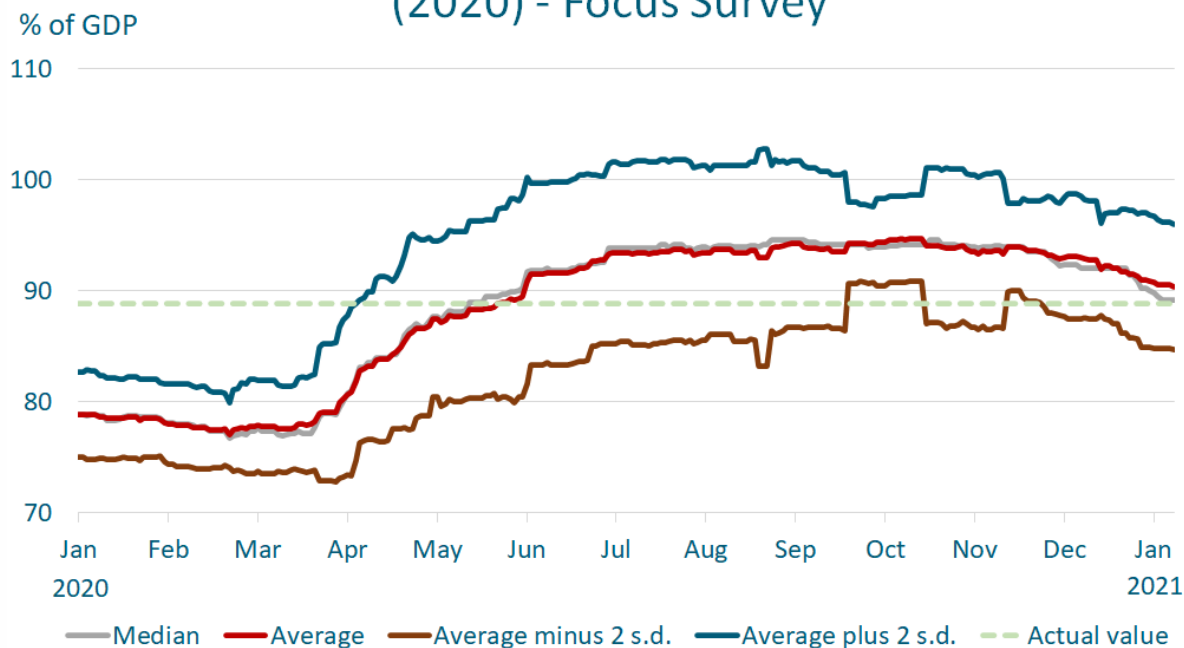
Source: IMF Fiscal Monitor April 2021. Database of Country Fiscal Measures in Response to the COVID-19 Pandemic; and IMF staff estimates.



# Public debt has increased, although less than expected

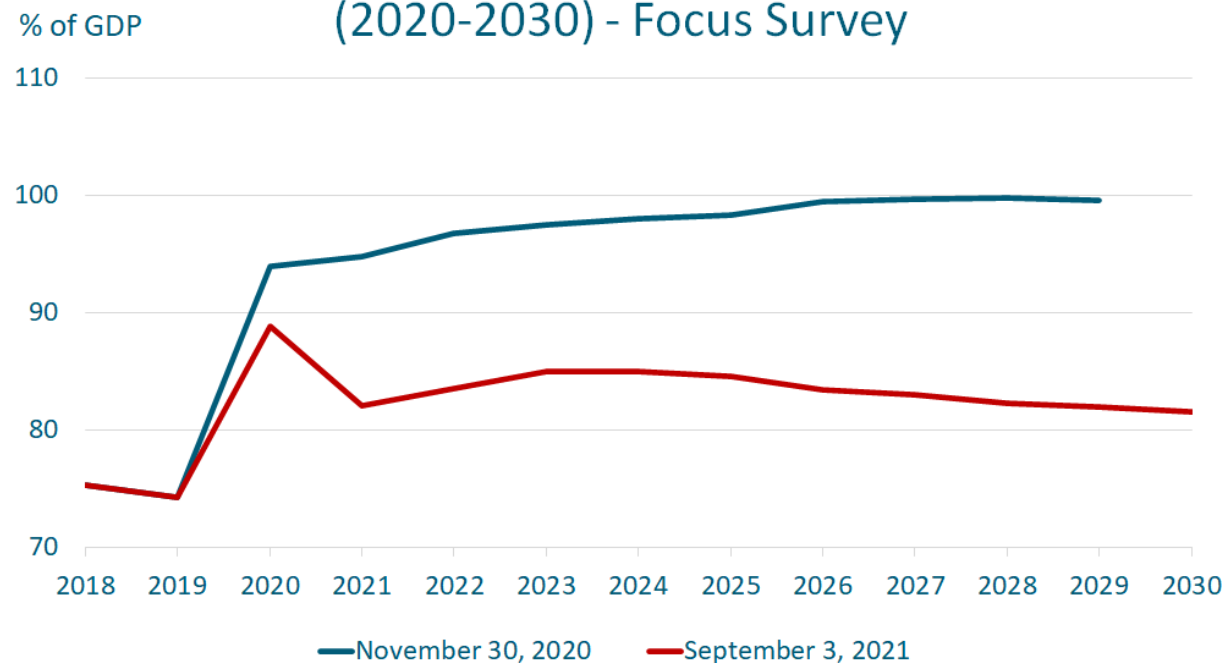
- Gross-government-debt-to-GDP ratio went to 88.8% in 2020 from 74.3% in 2019
- Consensus forecasts peaked at 94.6%

Expectations for gross government debt (2020) - Focus Survey



Source: BCB (Focus Survey).

Expectations for gross government debt (2020-2030) - Focus Survey

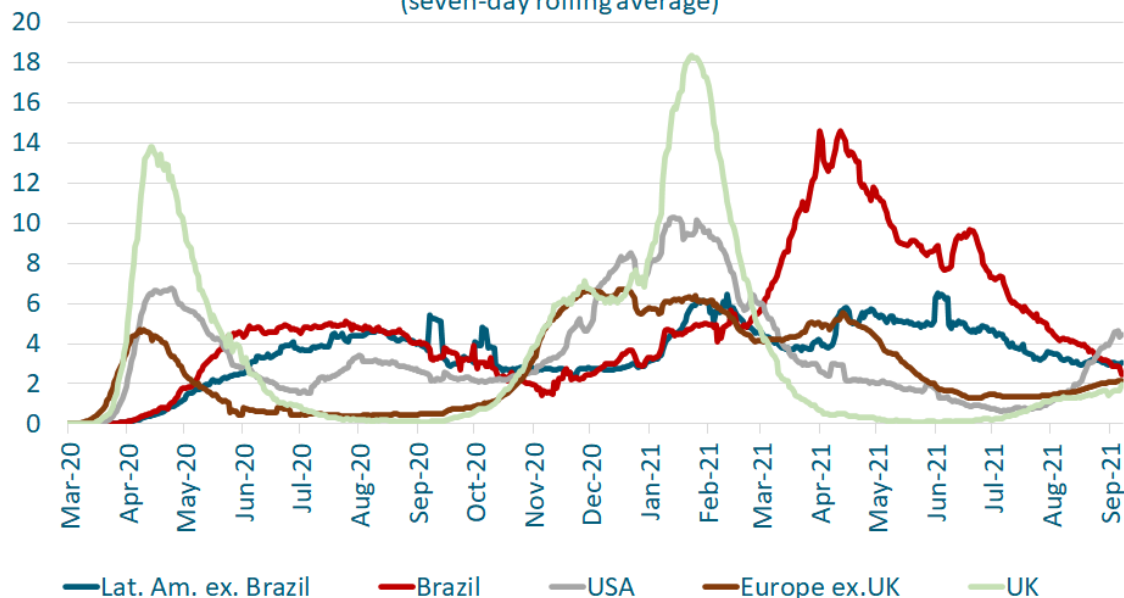


Source: BCB (Focus Survey).

# Vaccination has accelerated

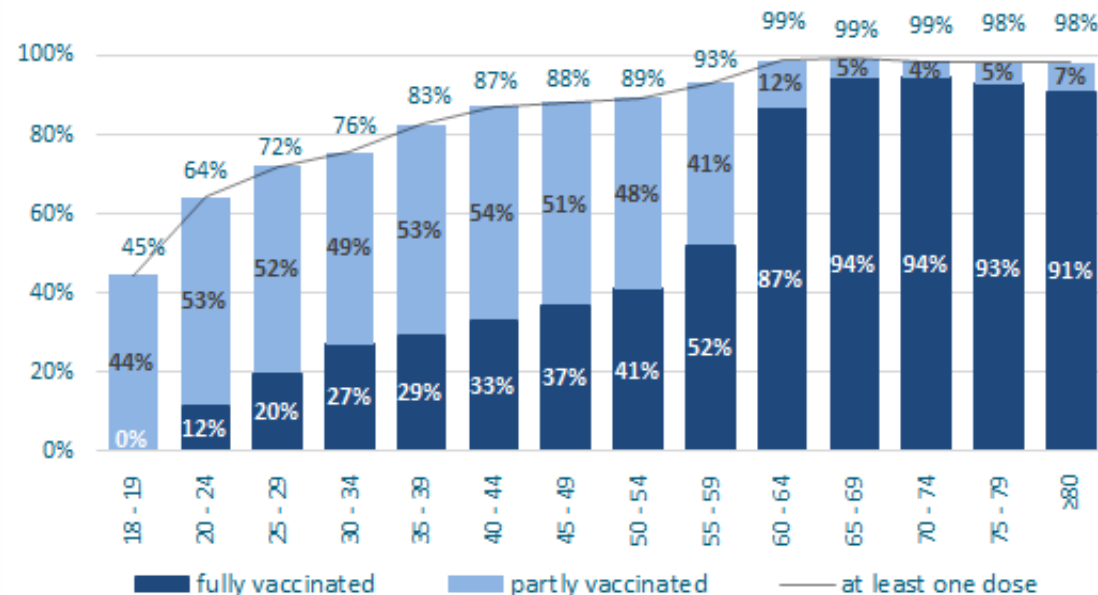
- Pandemic has receded significantly recently
- Most of adult population has received at least one dose

Covid: New deaths per million people  
(seven-day rolling average)



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

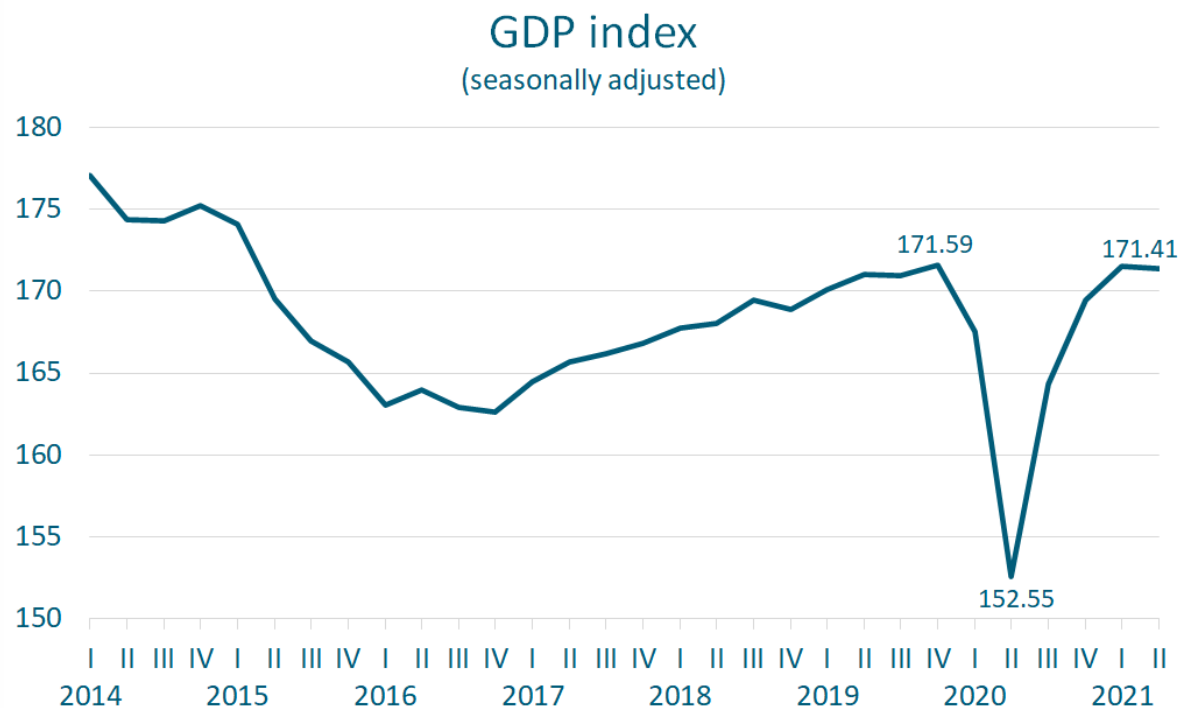
Brazil: Vaccination by age (% of population)



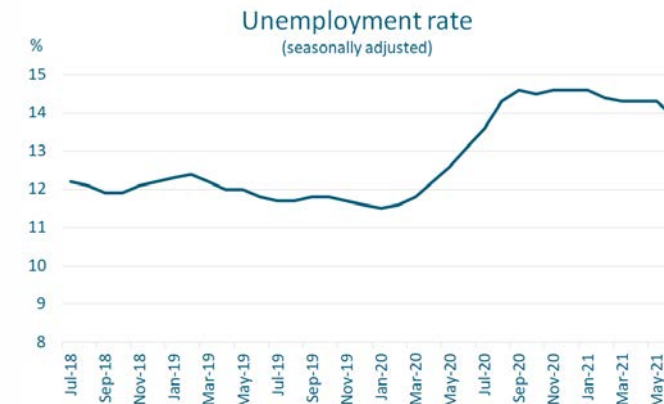
Note: Last data point: September 8, 2021.  
Source: Ministry of Health.

# Brazilian economic recovery

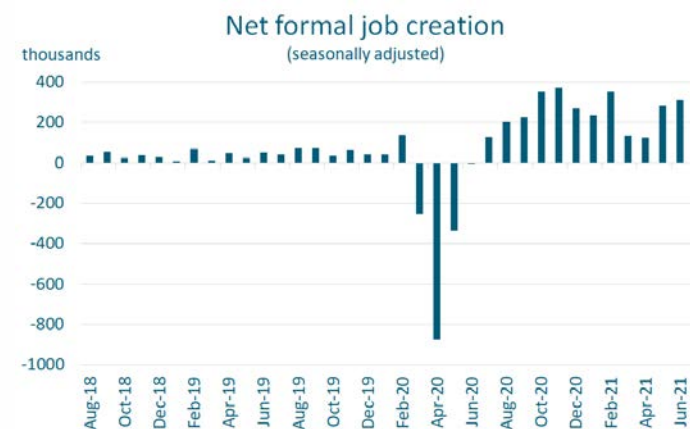
- V-Shaped recovery: GDP at the same level as the pre-pandemic level
- Labor market recovering, but its strength with mixed signals



Source: IBGE.



Source: IBGE; BCB



Source: Ministry of Labor; BCB

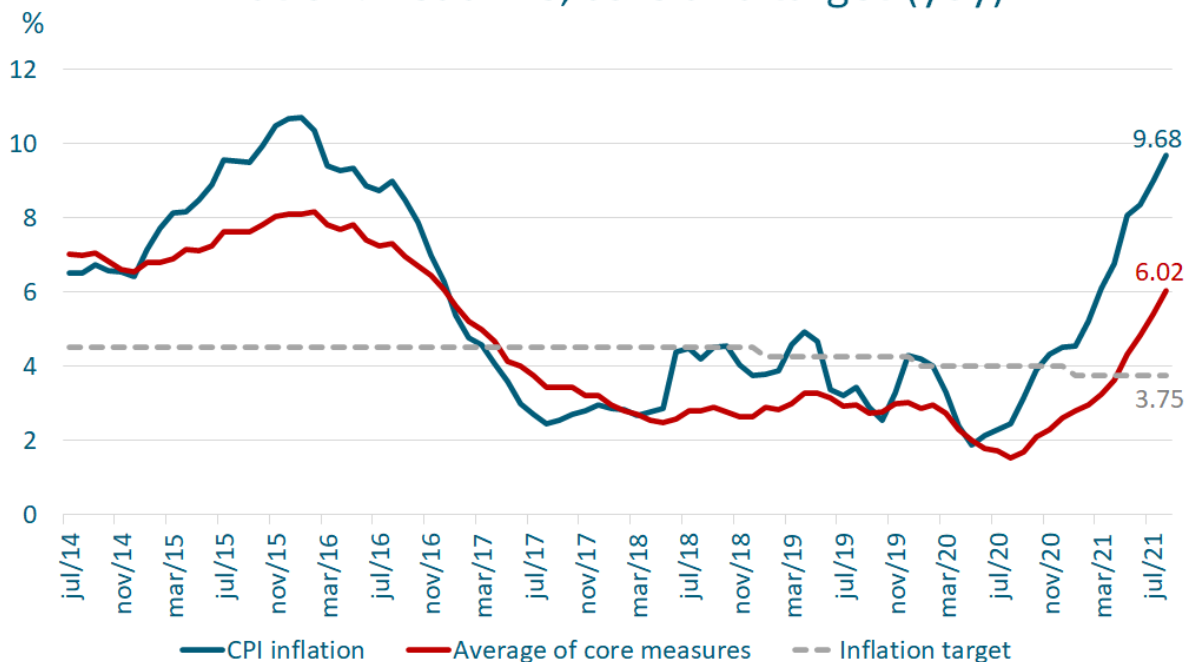
# Inflation pressures

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

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

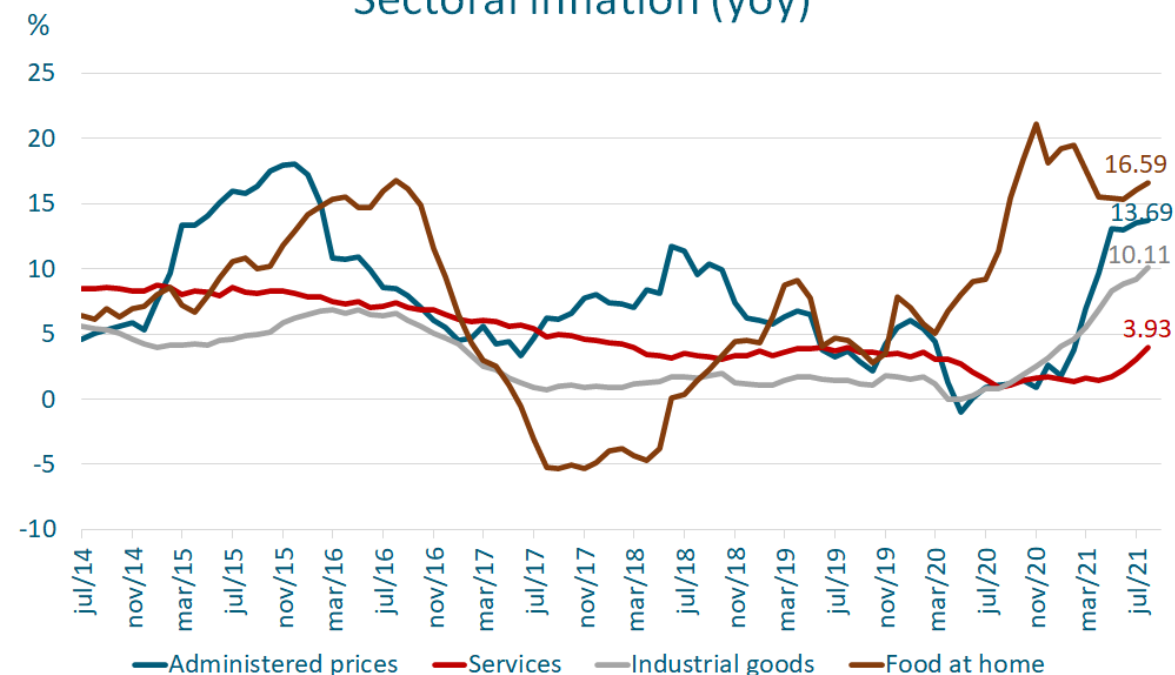
Gasoline	39.09
Bottled gas	31.07
Electricity	21.08

Inflation: Headline, core and target (yoy)



Source: IBGE; BCB.

Sectoral inflation (yoy)

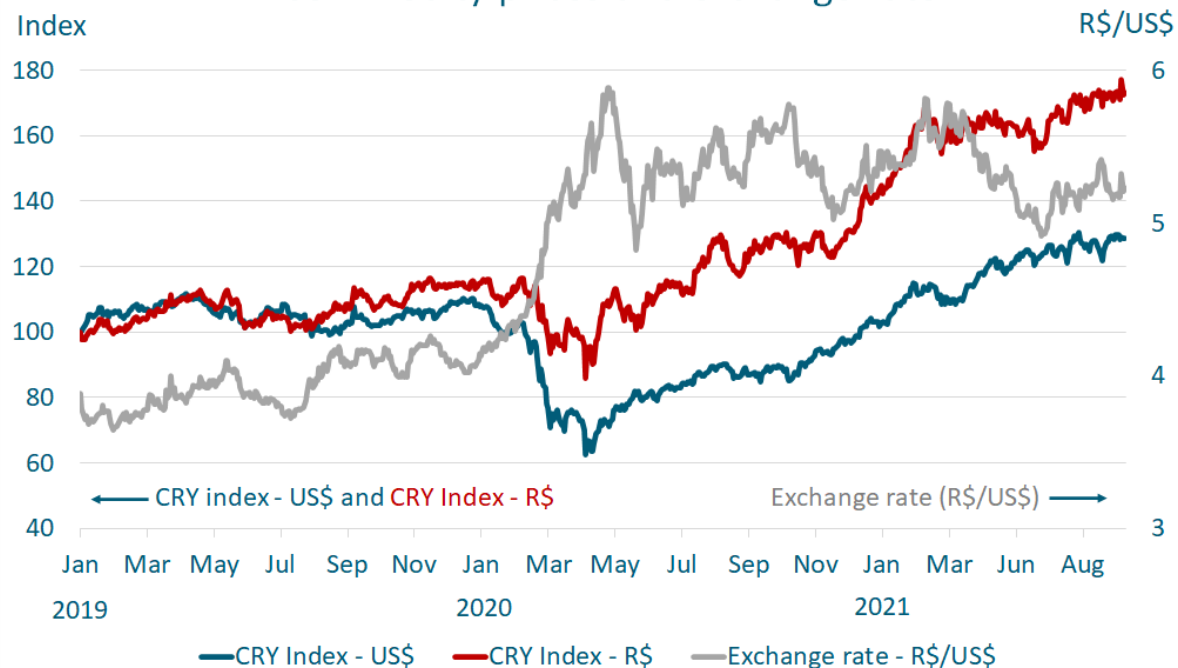


Source: IBGE; BCB.

# 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

Commodity prices and exchange rate

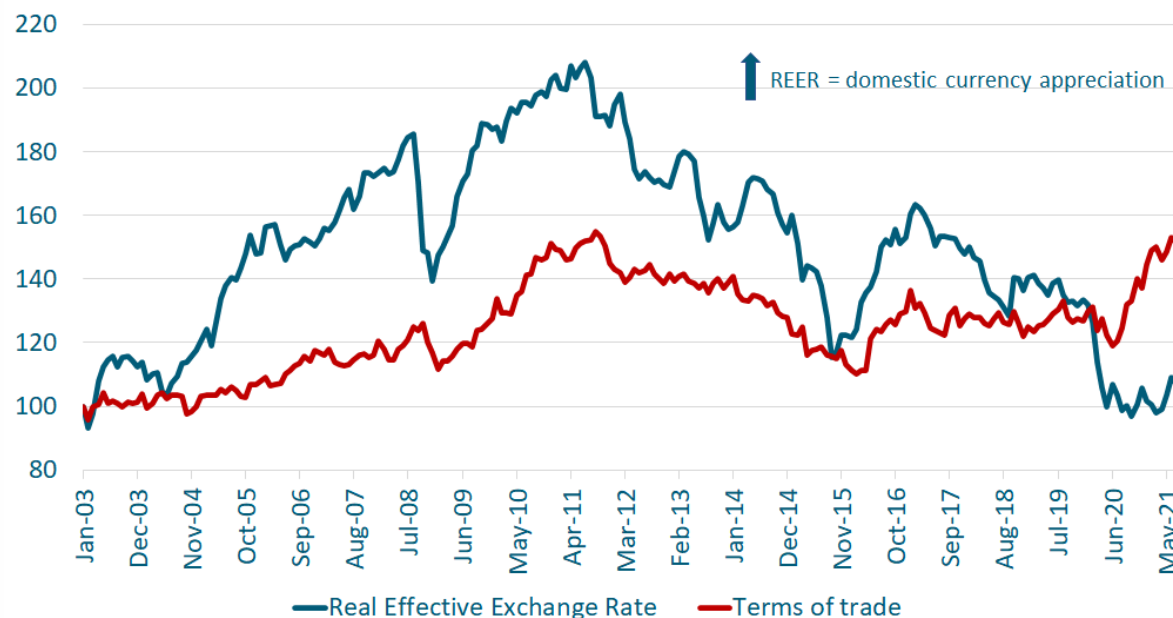


Note: CRY – US\$, CRY – R\$ (Jan 1, 2019 = 100)

Source: Bloomberg; BCB

Terms of trade and real effective exchange rate

(indexes, Jan/03 = 100)



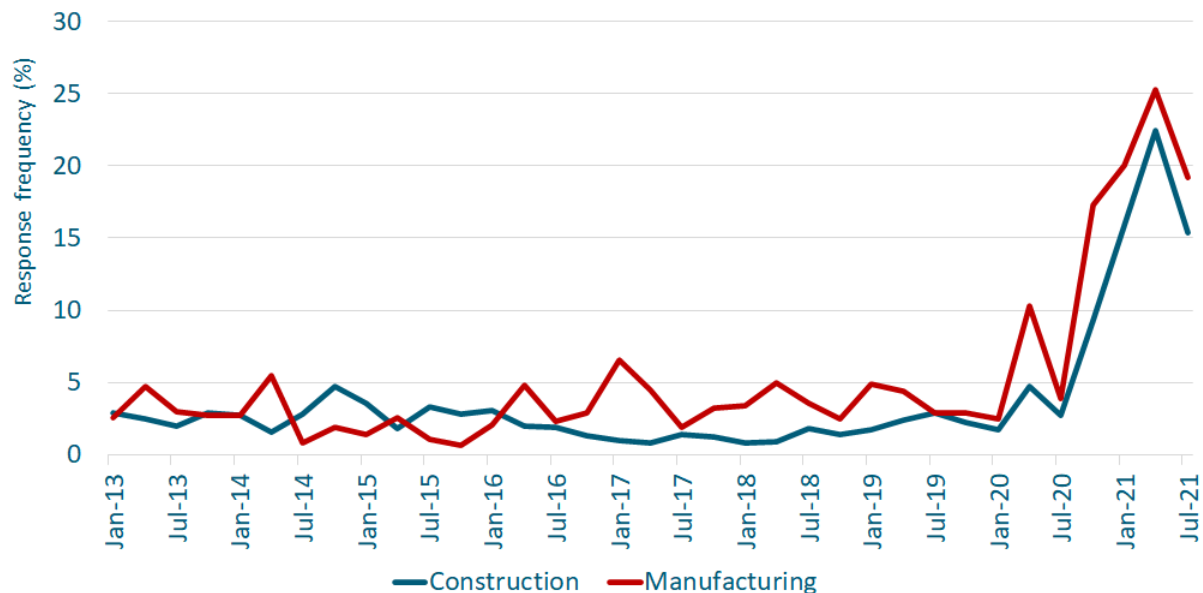
Note: CRY – US\$, CRY – R\$ (Jan 1, 2019 = 100)

Source: Secex; BCB

# Sectoral bottlenecks and energy crisis

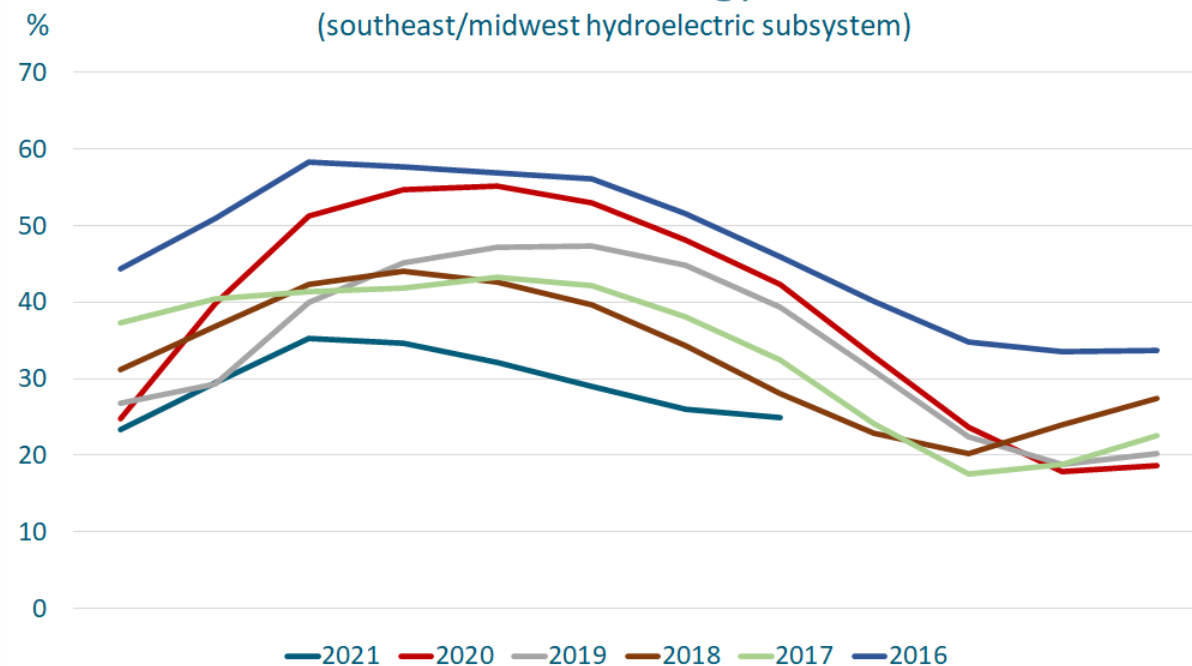
- Some sectors facing shortage of raw materials, affecting the production
- Drought leading to energy crisis, resulting in substantial increase in electricity prices

Restrictive factors for production:  
Raw material shortage



Source: FGV.

Stored energy  
(southeast/midwest hydroelectric subsystem)

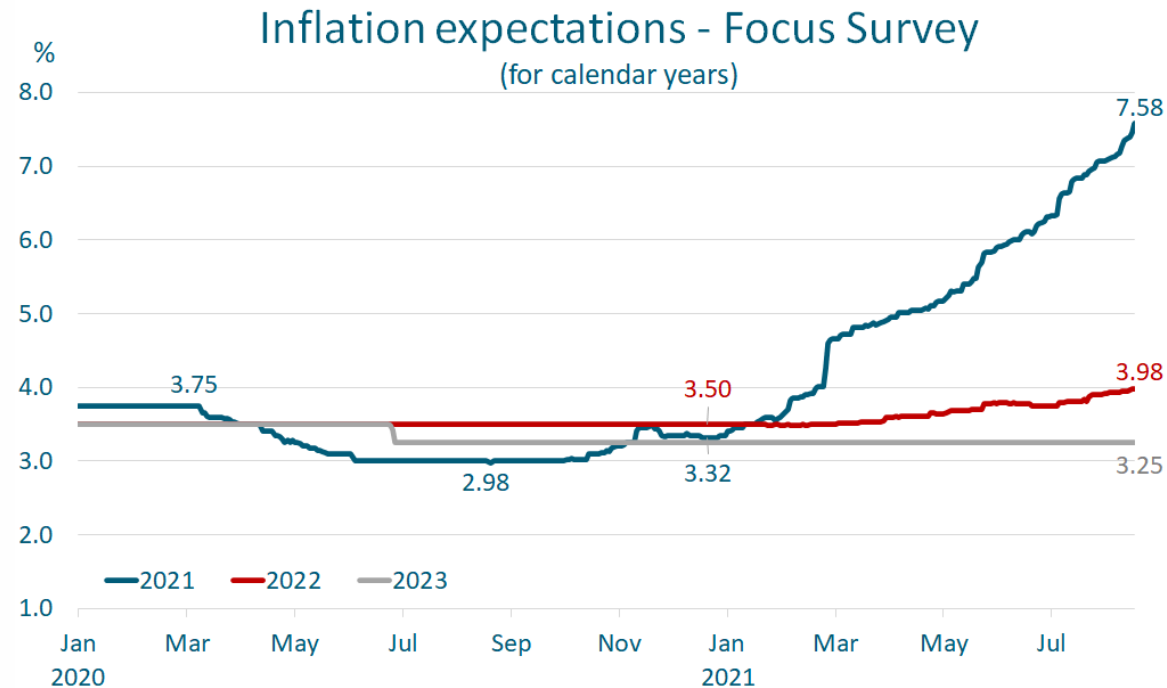
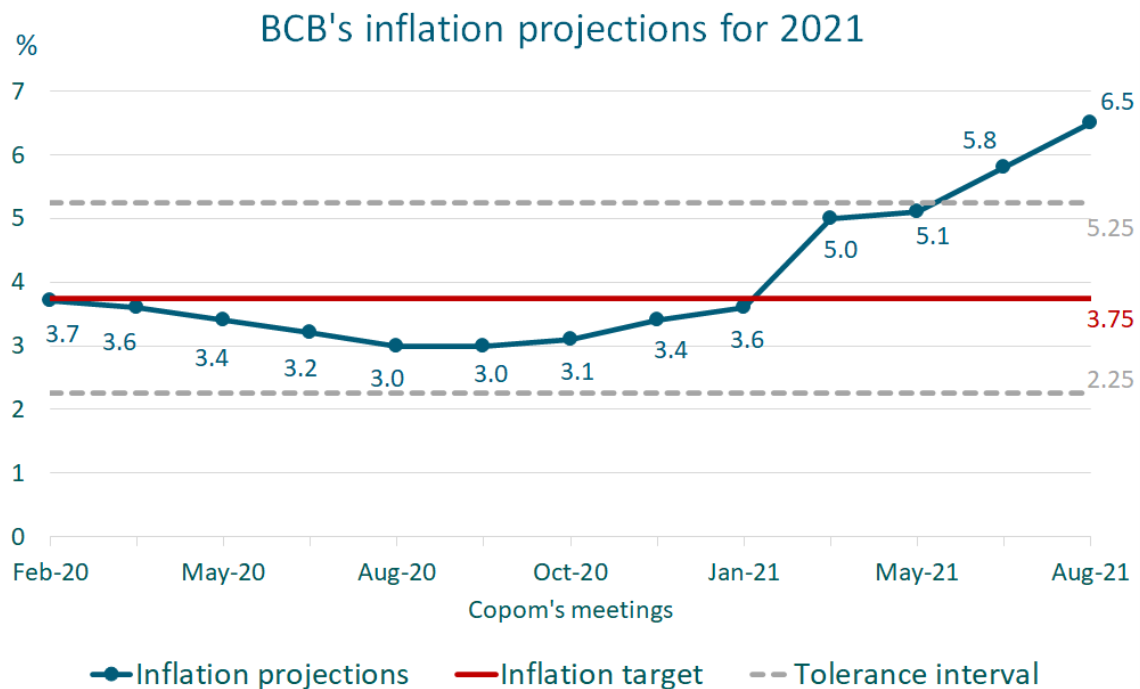


Source: ONS.

# Rise in inflation projections and agents' expectations

- Above the upper limit of the tolerance interval for 2021

Inflation target	
2021	3.75
2022	3.50
2023	3.25



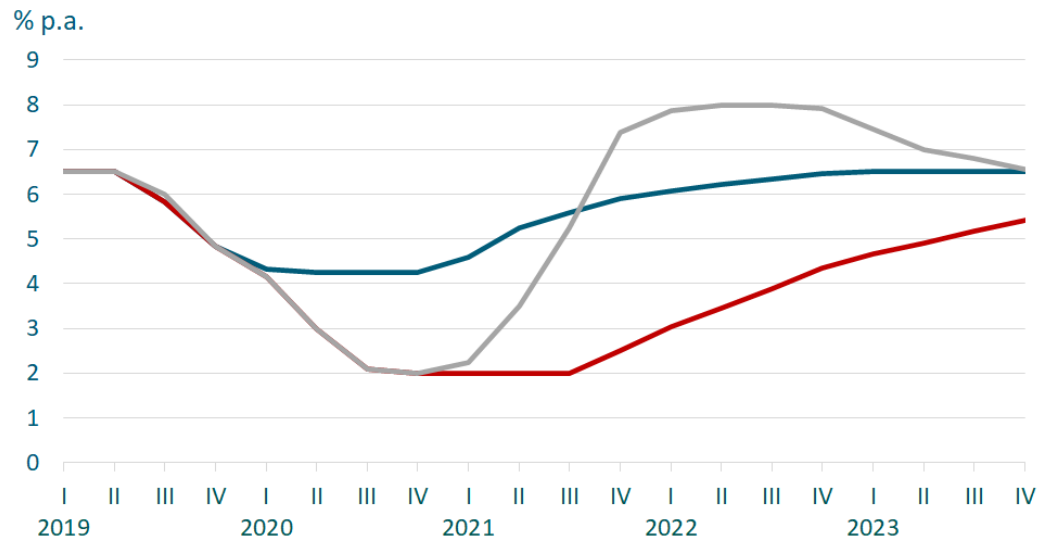
Source: BCB (Copom minutes).

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

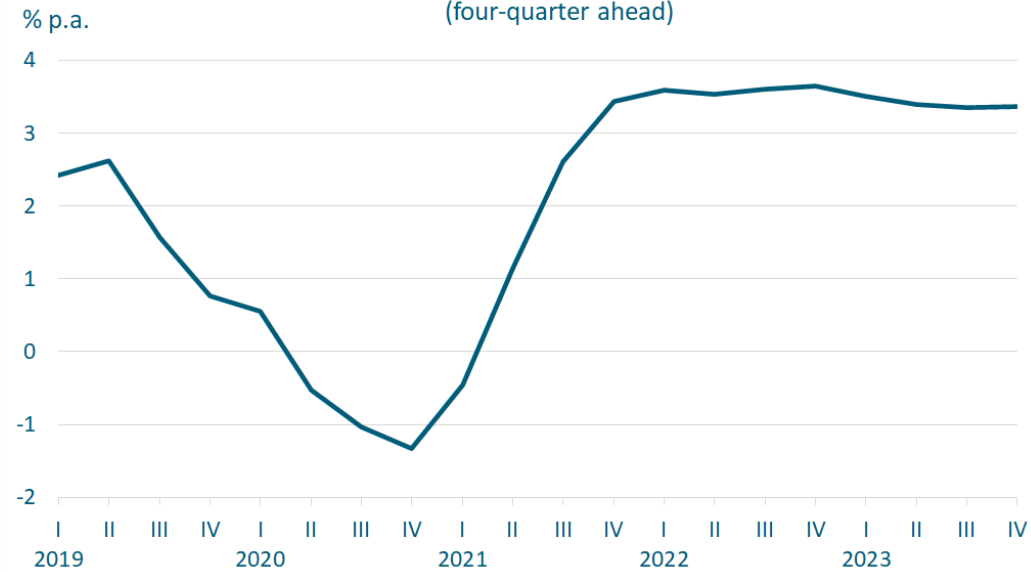


—Feb-20 Copom Meeting —Sep-20 Copom Meeting —Sep 3, 2021

Note: Feb-20 and Sep-20 Meetings refer to the Focus Survey on the previous Friday.  
Source: BCB (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