Selic policy rate to remain stable over the coming months

Overview

- **Central Bank statement reiterated that the benchmark Selic rate will remain steady in the coming months.** The minutes of the last meeting of the Monetary Policy Committee (Copom) and the fourth-quarter Inflation Report reinforced the message contained in the statement suggesting that benchmark rate will remain at 6.50% for now. The Central Bank acknowledged an improving inflation outlook and a more positive balance of risks, but suggested that upward risks remain relevant and will carry more weight. The models featured in the report suggest that, with the benchmark rate reaching 8.0% and the exchange rate at BRL/USD 3.85, inflation will remain within the bounds of the target range, even in the medium term. Lastly, the monetary authority said that caution, serenity and perseverance have been key in its efforts to keep inflation moving towards its targets. Considering our base scenario (which does not foresee any new shocks that could tilt the balance of risks to inflation) and the statement issued by the Copom, we believe the benchmark Selic rate will remain unchanged throughout the first half of 2019, with a gradual tightening cycle starting late in the third quarter and leading to a YE policy rate of 7.25%.
- **The mid-month inflation report (IPCA-15) for December continued to suggest a benign inflation outlook. I**nflation was negative at -0.16%, in line with our forecast (-0.17%) and below median market expectations (-0.12%). Core inflation remains well-behaved. On average, core prices have risen 2.4% in the last 12 months, below the lower bound of the inflation target (3.0%). We expect consumer inflation (IPCA) to come in at 4.0% in 2019.
- **In the same vein, current economic activity data continue to point to a gradual recovery.** The Central Bank's economic activity index (IBC-Br) remained practically steady between September and October. Together with other published indicators, the result suggests that the GDP will grow 0.1% in the fourth quarter. Nonetheless, other indicators such as business and consumer confidence and the formal labor market have signaled a positive transition to 2019. Net job creation (seasonally adjusted) stood at 73,000 formal jobs in November according to the Caged database of the Ministry of Labor, matching the average level for the past 3 months. In line with these developments, we forecast GDP to grow 1.1% in 2018 and 2.8% in 2019.
- **The FOMC raised the interest rate, but gave signs that the end-point of the cycle could be lower.** The Fed's monetary policy committee recognized that slower global growth and tighter financial conditions could translate into moderate growth for the U.S. economy in the future. As a result, it revised its GDP growth forecasts to 3.0% in 2018 and 2.3% in 2019, and the inflation forecast to 1.9% for both years. In the same vein, long-term forecasts were revised to 2.75%. Nonetheless, the Fed reiterated its previous assessment that the economy continues to grow at a strong pace, with a strong job market but inflation close to the 2.0% target. Thus, we believe that we are now more likely to see only one additional interest rate increase in 2019, compared to our previous forecast of two more increases.
- **Italy's budget was approved with a deficit target of 2.04% of GDP for 2019.** However, challenges remain despite the agreement reached between the Italian government and the European Commission, depending on the policy objectives.

Weekly Outlook

- **Unemployment rate, the General Market Price Index (IGP-M) and fiscal and credit reports are the highlights on the domestic agenda.** We expect the unemployment rate to confirm the gradual recovery of the labor market and decrease slightly in November, reaching 12.0% (seasonally adjusted). Influenced by the price of fuel and agricultural products, the IGP-M for December is likely to remain in negative territory, at -1.14%. Finally, we expect November's fiscal numbers to show a BRL 20 billion deficit, in line with the seasonal trend for the month. The Central Bank's credit report, in turn, is likely to show an increase in new loans, especially for individuals. **The international calendar will be empty next week.** The sole highlight is Germany's preliminary consumer inflation data, which is expected to remain benign.

Time	Country	Event	Forecast (Bloomberg)	Forecast (Depec)
Monday 12/24				
15:00	Brazil	MDIC: Trade Balance (weekly)		
Tuesday 12/25				
-	Brazil	National Holiday - Markets Closed		
Wednesday 12/26				
08:00	Brazil	FGV: Consumer Price Index (IPC-S) (weekly)		
08:00	Brazil	FGV: Retail Confidence (Dec)		
08:00	Brazil	FGV: Construction Confidence (Dec)		
08:25	Brazil	BCB: Focus Survey (weekly)		
12:30	Brazil	BCB: Currency Flows (weekly)		
14:30	Brazil	Federal Debt Total (Nov)		
Thursday 12/27				
08:00	Brazil	FGV: Industrial Confidence (Dec)		
10:30	Brazil	BCB: Press Release - Monetary Policy (Nov)		
-	Brazil	Central Govt Budget Balance (Nov)		20.3 billions
11:30	USA	Initial Jobless Claims - Weekly		
13:00	USA	Consumer Confidence (Dec)	133.6	
Friday 12/28				
08:00	Brazil	FGV: Services Confidence (Dec)		
08:00	Brazil	FGV: IGP-M (Dec)		-1.14% (MoM)
09:00	Brazil	IBGE: Unemployment Change (Nov)	11.4%	11.6%
10:30	Brazil	BCB: Press Release - Fiscal Policy (Nov)		
11:00	Germany	CPI (Dec - P)	0.3% (MoM)	
During the week				
-	Brazil	CNI: Capacity Utilization (Nov)		
-	Brazil	Tax Collections (Nov)		

	2017	2018	2019
Consumer inflation - IPCA (%)	2.95	3.80	4.00
GDP growth (%)	1.1	1.1	2.8
Industrial Production (%)	2.5	1.5	3.0
Retail Sales (%)	4.0	5.5	5.5
Job Creation (in thousands)	263.5	1359.7	1288.1
Unemployment Rate (% of labor force, avg)	12.7	12.3	11.9
Outstanding Credit Growth (%)	-0.5	4.0	8.3
Trade Balance (USD bn)	64.0	57.1	56.1
Current Account (USD bn)	-9.8	-13.2	-13.5
Exchange Rate (BRL/USD, eop)	3.31	3.80	3.70
Selic Rate (%, eop)	7.00	6.50	7.25
Primary Balance (BRL bn)	-111	-116.9	-93.4

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