

Interest rate cuts looking more likely

Overview

- **With the economy sputtering, the effects of supply shocks on inflation fading, and the apparent progress of the government's reform package, the market has upped its bets for a new rate-cutting cycle before the end of the year.** We forecast the benchmark Selic rate to end the year at 5.75% (considering three 0.25 p.p. cuts in the second half).
- **The economy continues to grow at a modest pace in the second quarter.** Industrial output showed slight growth in April (0.3%). However, leading indicators so far suggest that the industrial sector will return to negative growth in May. These indicators have suggested that economic growth is likely to moderate this quarter. With that, we have cut our GDP growth forecast to 0.8% in 2019.
- **The outlook for inflation remains benign.** The latest indicators show that the shocks that affected inflation in the beginning of the year are dissipating. IPCA consumer inflation for the month of May came in below expectations at 0.13%. However, some underlying indicators have picked up recently. We see this as a temporary phenomenon, given that the acceleration is very concentrated, there will still be a considerable amount of slack in the economy, and expectations remain anchored. Amid this environment, we have cut our IPCA forecasts to 3.8% for both 2019 and 2020 (down from 4.0% and 3.9%, respectively).
- **The escalating trade war continues to spook markets worldwide, causing the global economy to lose momentum.** Activity indicators for April and May suggest that global GDP growth in the second quarter could fail to meet expectations set a few months ago. The U.S. labor market also slowed down in May, even though the unemployment rate remains low. The global economy's loss of traction has impacted the price of several commodities – starting with oil, which fell 15% in the past few weeks.
- **Major central banks have also expressed their concern.** Governor Mario Draghi indicated that the ECB will keep its accommodative stance for the foreseeable future. For now, Draghi believes that the impacts of the trade war are concentrated in the industrial sector, but there are lingering concerns over potential contagion to other sectors. In the United States, several Fed board members intensified warnings of overseas risks to the U.S. economy. Future yield curves have already priced in more than two interest rate cuts in 2019.

The week ahead

- **Retail and service indicators are the highlights on the Brazilian calendar for the upcoming week.** We expect retail to show a slight decline (-0.2%), while the service sector should experience a slight recovery. Together with the industrial sector's performance, the numbers suggest that the IBC-Br will decline by 0.3% in April.
- **Internationally, all eyes will be on activity indicators for the U.S. and China for the month of May.** The data is expected to show that the global economy continues to feel the effects of the trade war and has lost momentum in the second quarter. U.S. consumer inflation data will also be announced this week. The reading should confirm a benign inflation outlook for the U.S. economy.

Time	Country	Event	Forecast (Bloomberg)	Forecast (Depec)
Monday 06/10				
08:00	Brazil	FGV: Employment Indicators (May)		
08:00	Brazil	FGV: Consumer Price Index (IPC-5) (weekly)		
08:25	Brazil	BCB: Focus Survey		
-	Brazil	MDIC: Trade Balance (weekly)		
Tuesday 06/11				
05:00	Brazil	FIPE: Consumer Price Index (weekly)		
08:00	Brazil	FGV: IGP-M (1st preview) (Jun)		
09:00	Brazil	IBGE: Industrial Production - regional (Apr)		
09:00	Brazil	IBGE: Agricultural production Survey (May)		
22:30	China	CPI (May)		
-	USA	USDA: World Agricultural Supply and Demand Estimates		
Wednesday 06/12				
09:00	Brazil	IBGE: Retail sales (PMC) (Apr)		-0,2% (MoM)
12:30	Brazil	BCB: Currency Flows (weekly)		
09:30	USA	CPI (May)	0.1% (MoM)	
Thursday 06/13				
09:00	Brazil	IBGE: Services Sector Volume (PMS) (Apr)		1,0% (YoY)
03:00	Germany	CPI (May - F)	0.2% (MoM)	
06:00	Eurozone	Industrial Production (Apr)	-0.3% (YoY)	
09:30	USA	Initial Jobless Claims - Weekly		
20:00	Peru	Central bank meeting		2.75%
23:00	China	Industrial Production (May)	6.2% (YoY)	
23:00	China	Fixed Assets Investments (May)	6.1% (YoY)	
Friday 06/14				
08:00	Brazil	FGV: IGP-10 (Jun)		0.50% (MoM)
08:30	Brazil	BCB: Economic Activity Index (Apr)		-0,3% (MoM)
10:15	USA	Industrial Production (May)	0.2% (MoM)	
11:00	USA	University of Michigan Sentiment (Jun - P)	97	
During the week				
-	China	Trade Balance (May)		

	2017	2018	2019
Consumer inflation - IPCA (%)	2.95	3.75	3.80
GDP growth (%)	1.1	1.1	0.8
Industrial Production (%)	2.5	1.1	0.6
Retail Sales (%)	4.0	5.0	4.5
Job Creation (in thousands)	264	1316	368
Unemployment Rate (% of labor force, avg)	12.7	12.3	12.9
Outstanding Credit Growth (%)	-0.5	5.0	7.5
Trade Balance (USD bn)	64.0	53.6	55.9
Current Account (USD bn)	-7.2	-14.5	-14.0
Exchange Rate (BRL/USD, eop)	3.31	3.87	3.80
Selic Rate (% eop)	7.00	6.50	5.75
Primary Balance (BRL bn)	-111	-108.3	-131
Gross Debt (% of GDP)	74.1	76.7	77.8

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