

Inflation continues to favor interest rate cuts by the Central Bank

Overview

- **Deflation should ramp up in the coming months.** The IPCA-15 recorded a drop of 0.01% in April. On the one hand, food prices rose 3.1%, especially fresh and industrialized food. However, the significant drop in the prices of industrial goods largely compensated for the unexpected food upswing and contributed to a new round of deceleration in core inflation, with a change of less than 1% (considering the average of the last 3 months, seasonally adjusted and annualized). The demand shock, therefore, is dictating price behavior for industrial goods and services, which will possibly continue to occur in the coming months, adding to the sharp drop in fuel prices. This environment of current inflation and expectations below the floor of the inflation target in 2020 continues to provide ample room for the Central Bank to proceed with interest rate cuts. We expect the Selic to close 2020 at 2.25%, remaining at this level next year.
- **Surveys of different sectors indicate an 8.5% retraction in the Brazilian second quarter GDP, in the year-over-year comparison.** The industry survey, for example, suggests a 16% year-over-year drop in industrial production. The service confidence index indicates an 11% downturn in revenues for the sector. The decline in consumer confidence, in turn, may translate into a negative impact of 8.5% on household consumption.
- **In the global economy, declining Covid-19 deaths tolls, advances regarding drug treatment and proposals to reopen economies have given some support to market prices.** Despite major volatility in international markets, the week showed some recovery in risky asset prices.
- **The U.S. first quarter GDP recorded an annualized drop of 4.8%, after climbing 2.1% in 4Q19.** Household consumption, which represents about 70% of the U.S. GDP, fell 7.6% in the first quarter. Non-residential investments and exports were also negatively affected. We expect an annualized drop of 35% for the second quarter and retraction of the American economy should reach 6% in 2020. In this scenario, the Fed showed caution regarding economic recovery and revealed a high willingness to act more, if necessary. The signal given by chairman Powell is that it will probably have to expand its actions, but there have been no changes thus far, either in the interest rate (already at 0%) or in the asset purchase program.
- **China showed accommodation this month, due to recovery resulting from the relaxation of several social distancing measures.** The manufacturing sector's PMI index dropped from 52 to 50.8 points between March and April. Euro Area GDP preview showed a 3.8% drop in the first quarter, with a negative highlight for the countries most affected by the pandemic (Italy, for example). At a meeting held today, the ECB reduced the TLTRO rate, signaled that low interest rates will remain at the current level – which can be further reduced – and reinforced that the asset purchase program will remain active for as long as necessary.

The week ahead

- **In Brazil, April's interest rate and inflation decisions will be the highlights of next week.** The Central Bank of Brazil is expected to continue the interest rate cut cycle by possibly making an additional 0.75 p.p. cut. The April IPCA, in turn, will intensify the deflation pace with a 0.26% drop. Industrial production will also be disclosed and should contract on the margin.
- **The international agenda includes interest rate decisions in England, several April surveys and U.S. employment.** The ISM services index is expected to show a significant drop and U.S. job market data will continue to show a significant destruction of vacancies.

Time	Country	Event	Forecast (Bloomberg)	Forecast (Depec)
Monday 05/04				
08:25	Brazil	BCB: Focus Survey		
10:00	Brazil	Markit: PMI Manufacturing (Apr)		
10:00	Brazil	CNI: Capacity Utilization (Mar)		
15:00	Brazil	MDIC: Trade Balance - monthly (Apr)		
--	Brazil	Fenabrave: Vehicle sales (Apr)		
Tuesday 05/05				
05:00	Brazil	FIPE: Consumer Price Index - monthly (Apr)		
09:00	Brazil	IBGE: Industrial Production (PIM) (Mar)		
05:30	United Kingdom	Markit: Composite PMI (Apr - F)		
11:00	USA	ISM Services (Apr)	41	
Wednesday 05/06				
10:00	Brazil	Markit: PMI Services (Apr)		
14:30	Brazil	BCB: Currency Flows (weekly)		
14:30	Brazil	BCB: Commodity Price Index		
10:00	Brazil	Markit: PMI Services (Apr)		
--	Brazil	BCB: Central bank meeting	3.25%	3.25%
05:00	Eurozone	Markit: Composite PMI (Apr - F)		
09:15	USA	Employment Change (ADP) (Apr)	-21000 k	
18:00	Chile	Central bank meeting	0.50%	0.50%
00:00	China	Trade Balance (Apr)	US\$ 9,06 bn	
Thursday 05/07				
11:30	Brazil	Anfavea: Vehicle Production (Apr)		
03:00	Germany	Industrial Production (Mar)		
08:00	United Kingdom	Central bank meeting	0.10%	0.10%
09:30	USA	Initial Jobless Claims - Weekly		
20:00	Peru	Central bank meeting	0.25%	0.25%
Friday 05/08				
08:00	Brazil	FGV: IGP-DI (Apr)		
09:00	Brazil	IBGE: Consumer Price Index (IPCA) (Apr)		
09:30	USA	Change in Nonfarm Payrolls (Apr)	-22 000 k	
09:30	USA	Unemployment Rate (Apr)	16.3%	

	2017	2018	2019	2020
GDP growth (%)	1.3	1.3	1.1	-4.0
Consumer inflation - IPCA (%)	2.95	3.75	4.3	2.2
Wholesale inflation - IGP-M (%)	-0.5	7.5	7.3	4.6
Selic Rate (% eop)	7.00	6.50	4.50	2.25
Exchange Rate (BRL/USD, eop)	3.31	3.87	4.03	4.90
Industrial Production (%)	2.5	1.0	-1.1	-3.0
Retail Sales (%)	4.0	5.0	3.9	-6.5
Job Creation (in thousands)	1899	966	1816	-1418
Unemployment Rate (% of labor force, avg)	12.7	12.3	12.1	13.7
Outstanding Credit Growth (%)	-0.5	5.1	6.5	1.0
Trade Balance (USD bn)	64.0	53.0	39.4	43.4
Current Account (USD bn)	-15.0	-41.5	-50.8	-27.6
Primary Balance (BRL bn)	-111	-108.3	-62	-645
Gross Debt (% of GDP)	74.1	76.5	75.8	89.9

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