

## Plenty of room for Selic rate cuts ahead

### Overview

- **The Monetary Policy Committee (Copom) cut the Selic rate by 0.75 pp, signaling that there is room for more cuts of the same magnitude at the next meeting.** By bringing the benchmark rate down to 3.0% per year, the Committee acknowledged that the effects of the pandemic have created a very challenging global environment. With inflation forecasts below the 2020 and 2021 targets, the Central Bank believes that there is room for “extremely high” monetary stimulus, but the option for a smaller cut than prescribed by the forecasting models stems from the level of uncertainty about the environment. One risk factor that often comes up is the fiscal deterioration brought on by the efforts against the pandemic, with a possible upward impact on structural interest.
- **Despite the uncertainties, we cannot rule out a terminal Selic rate below 2.25% per year, which is our current scenario.** These uncertainties will not go away anytime soon, but we estimate there is room for a 1.75%-2.25% interest rate at the end of the current cycle. The exchange rate continues to bring significant upside risk to prices. Commodity prices in BRL continue to rise steadily. These movements have occurred despite the disinflationary bias of international commodity prices, which are still present despite the upward adjustment in oil prices. On the other hand, domestic activity and inflation data support the downward trend of the Selic rate. Manufacturing output fell 9.1% in March, while car sales dropped 59% on the margin in April. The IPCA came in at -0.31% in April, with core prices decelerating sharply.
- **Amid this backdrop, new stimulus measures are implemented, with their respective fiscal impacts.** Congress passed the Wartime Budget bill, which authorizes the Central Bank to purchase government bonds and private assets, and provides a financial aid package to states and municipalities, which includes transfers and the suspension of debt payments to the Federal Government. We believe that the ongoing fiscal deterioration, mentioned by Fitch as the main reason for changing Brazil’s rating bias to negative, will be limited to the duration of the pandemic. Another factor to be taken into consideration in the discussions about Brazil’s vulnerabilities is that the currency depreciation has adjusted our net foreign liabilities. Depending on the exchange rate’s trajectory, the current account could be balanced as early as the second half of 2021.
- **The service sector and the labor market continue to be more impacted by the pandemic than manufacturing, which is also experiencing a downturn.** The PMI for several countries reinforce this view, contrary to what happened in 2019 with the trade war, when manufacturing was the hardest hit industry. In the U.S., the unemployment rate reached an all-time high in April at 14.7% (vs 4.4% in March), with a net loss of 20.5 million jobs for the month. As more economies get ready to restart over the next few weeks, and if there aren’t any major setbacks in that process, we are likely to see a partial rebound from this downturn in upcoming data releases.

### The week ahead

- **In Brazil, Monetary Policy Committee (Copom) meeting minutes and activity indicators are on the radar.** The Central Bank’s document may provide more signals about how much room it has for additional rate cuts. Retail and services data for March will provide clearer insight into first-quarter GDP figures.
- **U.S.-China meeting highlights the coming week’s schedule, with tensions once again escalating between both countries.** Activity indicators will also be announced: April’s manufacturing output in both China and the U.S., and first-quarter GDP in Europe.

Time	Country	Event	Forecast (Bloomberg)	Forecast (Depec)
<b>Monday 05/11</b>				
08:25	Brazil	BCB: Focus Survey		
15:00	Brazil	MDIC: Trade Balance (weekly)		
22:30	China	CPI (Apr)	3.7% (y/y)	
<b>Tuesday 05/12</b>				
05:00	Brazil	FIPE: Consumer Price Index (weekly)		
08:00	Brazil	BCB: Copom minutes		
08:00	Brazil	FGV: IGP-M (1st preview) (May)		
08:00	Brazil	IBGE: Agricultural production Survey		
09:00	Brazil	IBGE: Services Sector Volume (PMS) (Mar)		
09:00	Brazil	Conab: 8th Grains crop survey 2019/2020		
09:30	USA	CPI (Apr)	-0.7% (m/m)	
-	USA	USDA: World Agricultural Supply and Demand Estimates		
<b>Wednesday 05/13</b>				
09:00	Brazil	IBGE: Retail sales (PMC) (Mar)		
03:00	United Kingdom	GDP (1Q - P)	-1.9% (q/q)	
06:00	Eurozone	Industrial Production (Mar)		
<b>Thursday 05/14</b>				
09:00	Brazil	IBGE: Industrial Production - regional (Mar)		
14:30	Brazil	BCB: Currency Flows (weekly)		
03:00	Germany	CPI (Apr - F)	0.3% (m/m)	
09:30	USA	Initial Jobless Claims - Weekly		
15:00	Mexico	Central bank meeting	5.50%	5.50%
23:00	China	Fixed Assets Investments (Apr)	-9.0%	
23:00	China	Industrial Production (Apr)	-4.8% (y/y)	
<b>Friday 05/15</b>				
09:00	Brazil	BCB: Economic Activity Index (Mar)		
03:00	Brazil	IBGE: Quartely employment survey (1Q)		
03:00	Germany	GDP (1Q - P)	-2.0 (q/q)	
06:00	Eurozone	GDP (1Q - P)		
09:30	USA	Índice Empire Manufacturing de atividade (May)	-64	
10:15	USA	Industrial Production (Apr)	-11.0% (m/m)	
11:00	USA	University of Michigan Sentiment (May - P)	67,5	
13:00	Colombia	GDP (1Q)		3.8% (y/y)
<b>During the week</b>				
10:00	Brazil	CNI: Capacity Utilization		

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

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