

Inflation continues to give the Central Bank room to cut interest rates

Overview

- **Weak demand has been the main determinant of inflation, despite some occasional shocks.** The Broad Consumer Inflation Index (IPCA) came in at -0.38% in May, as the underlying core and service prices eased significantly. Now, average core inflation (seasonally adjusted and annualized) came in at -0.8% in the last 3 months. It is worth noting that some durable goods saw large price increases, and therefore deserves close attention as how the exchange rate and commodity price pass-through unfolds in upcoming releases. In any case, core prices are expected to remain in deflationary territory in June and July, even if headline inflation spikes due to regulated price surges (especially for gasoline).
- **Job market indicators point to persistently high unemployment figures in the short term.** The FGV Coincident Unemployment Indicator rose in May, suggesting an increase in the unemployment rate. Unemployment filings reached 960,000 in May, totaling 1.9 million during the pandemic. In other words, the weaker job market should continue to hold back any recovery in household consumption.
- **Despite better than expected economic data coming from the U.S. last week, the Fed has signaled that it will maintain an accommodative monetary policy for a long time.** The FOMC meeting this week brought no surprises: U.S. interest rates remain at zero. However, attention turned both to the projections (which not been updated since December) and to the tone of Fed Chairman Jerome Powell's statement and speech. The Fed now anticipates a 6.5% drop in U.S. GDP in 2020 and a 5% increase in 2021. Inflation was projected at 0.8% in 2020, 1.6% in 2021 and 1.7% in 2022, which would make it 3 consecutive years of inflation running at below the 2% target, while unemployment will remain high (from 9.3% in 2020 to 5.5% in 2022). In other words, the Fed continues to expect an extremely challenging scenario over the next two and a half years, despite some better-than-expected economic data recently – which warrants keeping interest rates low for a long time.
- **After the Fed statement, markets adopted a more cautionary view of the global economic recovery** This view is supported by newly released OECD projections, which has world GDP shrinking 6% in 2020, before bouncing back to 5.2% growth in 2021. There is also fear of a second wave of coronavirus infections, and we therefore agree with the view that the next 1-2 months will be important for calibrating expectations about the pace of recovery as economies begin to reopen.

The week ahead

- **The Monetary Policy Committee (Copom) meeting is the highlight on the domestic calendar.** We expect the benchmark Selic rate to be trimmed by 0.75 p.p. Well-behaved current inflation, along with a slowdown in core prices and an expected lowering of BCB-model inflation projections at this next meeting should be enough to warrant a rate cut at the upcoming meeting. We will get the numbers for retail and service sales for April, which are expected to show the negative impacts of the pandemic in that month.
- **The Bank of England and Bank of Japan will announce their monetary policy decisions,** with both expected to follow in the Fed's footsteps. The mid-month PMI readings for June will be crucial to let us know whether last month's positive trend was maintained. Also on the radar are the manufacturing output figures from the U.S. and China (both for the month of May).

Time	Country	Event	Forecast (Bloomberg)	Forecast (Depec)
Monday 06/15				
08:25	Brazil	BCB: Focus Survey		
15:00	Brazil	MDIC: Trade Balance (weekly)		
09:30	USA	Índice Empire Manufacturing de atividade (Jun)	-27.5	
--	Japan	Central bank meeting	-0.10%	
23:00	China	Fixed Assets Investments (May)	-6.0%	
23:00	China	Industrial Production (May)	-2.8% (YoY)	
*The indicator will be released on June, 14th				
Terça-Feira 16/06				
08:00	Brazil	FGV: IGP-10 (Jun)		1.46% (MoM)
09:00	Brazil	IBGE: Retail sales (PMC) (Apr)		
03:00	Germany	CPI (May - F)	-0.1% (MoM)	
06:00	Germany	ZEW Survey Expectations (Jun)	55.5	
10:15	USA	Industrial Production (May)	2.9% (MoM)	
19:00	Chile	Central bank meeting	0.50%	0.50%
Wednesday 06/17				
05:00	Brazil	FIPE: Consumer Price Index (weekly)		
9:00	Brazil	IBGE: Services Sector Volume (PMS) (Apr)		
14:30	Brazil	BCB: Currency Flows (weekly)		
-	Brazil	BCB: Central bank meeting	2.25%	2.25%
06:00	Eurozone	CPI (May - F)		
Thursday 06/18				
08:00	Brazil	FGV: IGP-M (2nd preview) (Jun)		
09:00	Brazil	BCB: Economic Activity Index (Apr)		
08:00	United Kingdom	Central bank meeting	0.10%	
09:30	USA	Initial Jobless Claims - Weekly		
09:30	USA	Fed Philadelphia Outlook (Jun)	-25.0	
Friday 06/19				
--	Brazil	CNI: Industrial Confidence (May)		
During the week				
--	Brazil	Tax Collections (May)		

	2017	2018	2019	2020
GDP growth (%)	1.3	1.3	1.1	-5.9
Consumer inflation - IPCA (%)	2.95	3.75	4.3	1.5
Wholesale inflation - IGP-M (%)	-0.5	7.5	7.3	5.1
Selic Rate (% eop)	7.00	6.50	4.50	2.25
Exchange Rate (BRL/USD, eop)	3.31	3.87	4.03	5.10
Industrial Production (%)	2.5	1.0	-1.1	-7.5
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	14.0
Outstanding Credit Growth (%)	-0.4	5.1	6.5	5.0
Trade Balance (USD bn)	64.0	53.0	39.4	50.5
Current Account (USD bn)	-15.0	-41.5	-50.8	-7.2
Primary Balance (BRL bn)	-111	-108.3	-62	-750
Gross Debt (% of GDP)	74.1	76.5	75.8	93.8

Technical Staff

Department of Economic Research and Studies Fernando Honorato Barbosa

Economists Andréa Bastos Damico / Ariana Stephanie Zerbinatti / Constantin Jancsó / Fabiana D'Atri / Myriã Tatianny Neves Bast / Priscila Pacheco Trigo / Robson Rodrigues Pereira / Thiago Coraucci de Angelis / Thomas Henrique Schreurs Pires

Interns Daniel Funari Fouto / Gustavo Rostelato de Miranda / Henrique Monteiro de Souza Rangel / Lucas Daniel Duarte / Lucas Oliveira Costa da Silva / Marcelo Henrique Leite Alonso

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