

# 240th

## Minutes of the Meeting of the **Monetary Policy Committee — Copom**

August 3-4, 2021

**Date:** August 3-4, 2021

**Place:** BCB Headquarters' meeting rooms on the 8<sup>th</sup> floor – Brasília – DF – Brazil

**Starting and ending times:** August 3: 10:19 AM – 1:41 PM; 3:05 PM – 7:11 PM  
August 4: 2:30 PM – 6:46 PM

**In attendance:**

**Members of the Copom**

Roberto Oliveira Campos Neto – *Governor*  
Carolina de Assis Barros  
Fabio Kanczuk  
Fernanda Magalhães Rumenos Guardado  
João Manoel Pinho de Mello  
Maurício Costa de Moura  
Otávio Ribeiro Damaso  
Paulo Sérgio Neves de Souza

**Department Heads in charge of technical presentations (August 3):**

Alan da Silva Andrade Mendes – *Department of Foreign Reserves*  
André Minella – *Research Department (also present on August 4)*  
André de Oliveira Amante – *Open Market Operations Department*  
Fabia Aparecida de Carvalho – *Department of International Affairs*  
Ricardo Sabbadini – *Department of Economics*  
Rogério Antônio Lucca – *Department of Banking Operations and Payments System*

**Other participants (August 3):**

Arnildo da Silva Correa – *Head of the Office of Economic Advisor*  
Eduardo José Araújo Lima – *Head of the Deputy Governor for Economic Policy's Office*  
Euler Pereira Gonçalves de Mello – *Deputy Head of the Research Department*  
Julio Cesar Costa Pinto – *Head of the Deputy Governor for Monetary Policy's Office*  
Leonardo Martins Nogueira – *Executive Secretary*  
Mariane Santiago de Souza – *Head of the Governor's Office*  
Olavo Lins Romano Pereira – *Deputy Head of the Department of International Affairs*  
Pedro Henrique da Silva Castro – *Deputy Head of the Department of Economics*

The members of Copom analyzed the recent performance and prospects for the Brazilian and international economies, under the monetary policy framework, whose objective is to comply with the inflation targets established by the National Monetary Council. This document represents Copom's best effort to provide an English version of its policy meeting minutes. In case of inconsistency, the Portuguese version prevails.

### **A) Update of economic outlook and Copom's baseline scenario<sup>1</sup>**

1. Regarding the global outlook, the evolution of the Covid-19 Delta variant adds risk to the recovery of the world economy. The Committee considers that, in spite of the recent movements in the yield curves, there is still a relevant upward inflation risk in the central economies. Nevertheless, the environment for emerging economies remains favorable with the long-lasting monetary stimuli, with the fiscal programs, and with the reopening of the major economies.
2. Turning to the Brazilian economy, recent indicators continue evolving satisfactorily and do not call for relevant revisions in growth forecasts, which display a robust economic recovery during the second half of the year.
3. The various measures of underlying inflation are above the range compatible with meeting the inflation target.
4. Inflation expectations for 2021, 2022, and 2023 collected by the Focus survey are around 6.8%, 3.8%, and 3.25%, respectively.
5. Consumer inflation has been persistent. Recent indicators show a worse composition. It is noteworthy the surprise with the underlying services inflation and the continuing pressure on industrial goods, which cause core measures to rise. Furthermore, there is new pressure in volatile components, such as the possible additional increase in electricity fares and food prices, both due to adverse weather conditions. Altogether, these factors imply significant revisions in short-term forecasts.
6. The Copom's inflation projections in its baseline scenario, with interest rate path extracted from the Focus survey and exchange rate starting at USD/BRL 5.15<sup>2</sup>, and evolving according to the purchase power parity (PPP), stand around 6.5% for 2021, 3.5% for 2022 and 3.2% for 2023. This scenario assumes a path for the Selic rate that rises to 7.0% p.a. in 2021, remains at this level during 2022 and drops to 6.5% p.a. during 2023. In this scenario, inflation projections for administered prices are 10.0% for 2021 and 4.6% for 2022 and 2023. The energy flag is assumed to be neutral, remaining at "red level 1" in December each year.

### **B) Risks around the baseline inflation scenario**

7. The Copom's baseline scenario for inflation encompasses risk factors in both directions.
8. On the one hand, a possible reversion, even if partial, of the recent increase in the price of international commodities measured in local currency would produce a lower-than-projected inflation in the baseline scenario.
9. On the other hand, further extensions of fiscal policy responses to the pandemic that increase aggregate demand and deteriorate the fiscal path may pressure the country's risk premium. Despite the recent improvement of debt sustainability indicators, the elevated fiscal risk creates an upward asymmetry in the balance of risks, *i.e.*, in the direction of higher-than-expected paths for inflation over the relevant horizon for monetary policy.

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<sup>1</sup> Unless explicitly stated otherwise, this update takes into account changes that occurred since the June Copom meeting (239<sup>th</sup> meeting).

<sup>2</sup> Value obtained according to the usual procedure of rounding the average USD/BRL exchange rate observed in the five business days ended in the last day of the week prior to the Copom meeting.

### C) Discussion about the conduct of monetary policy

10. Regarding the global outlook, the Committee assessed that the fiscal and monetary stimuli are promoting robust growth and that, henceforth, inflation dynamics in central and emerging economies should increasingly depend on demand channels. In this regard further discussions about the risk of a lasting inflation increase in the United States and the associated repricing of financial assets could turn the environment for emerging economies challenging.

11. The Copom members discussed the evolution of domestic economic activity in light of the available information and indicators. They considered that the latest available data continues to evolve positively, in line with growth forecasts. In the Committee's view, the second half of the year should bring a robust recovery, as the effects of the vaccination are felt more broadly. The Committee noticed that the median of growth forecasts in the Focus survey is appreciably more optimistic than those of its baseline scenario and pondered whether the difficulties related to seasonal adjustments due to the pandemic shock would explain this divergence.

12. The Copom members then debated the level of economic slack. Although the economic slack as a whole is quickly returning to the late 2019 level, the Committee considered that the pandemic still produces heterogeneous effects on economic sectors and, in particular, on the labor market, with consequences for the recent and prospective dynamics of inflation.

13. Next, the Copom discussed the implementation of monetary policy, considering not only the baseline scenario, but also the balance of risks for inflation. According to the baseline scenario, which uses the interest rate path extracted from the Focus survey, the exchange rate at purchasing power parity, and commodity prices in USD stable in real terms, the inflation projections are aligned to the targets for 2022 and 2023. The Committee judged that the fiscal risks continue to imply an upward bias in the projections. This asymmetry in the balance of risks affects the appropriate degree of monetary stimulus, thus justifying a path for monetary policy that is more restrictive than the one used in the baseline scenario.

14. Copom then evaluated different tightening paths for monetary policy. Considering the baseline scenario and the balance of risks, the Committee assessed that – should there be no changes in the inflation conditioning factors – subsequent uninterrupted interest rate increases are required up to a level above the neutral rate, to obtain projections around the inflation targets in the relevant horizon. Therefore, a tightening cycle of the policy rate to a level consistent with restrictive monetary policy has become appropriate. The Committee opted to communicate this decision, maintaining transparency about the monetary policy path implied in its projections, and reaffirming that this view will be systematically reassessed as changes in inflation determinants or in the balance of risks occur.

15. The Committee discussed potential explanations for the difference between its baseline scenario's projections and the inflation expectations extracted from the Focus survey. First, expectations may incorporate different assumptions about the determinants of inflation, such as administered prices and economic growth, as well as contain different perceptions on risk or alternative scenarios. Second, the long sequence of shocks and one-way revisions of expectations may increase the perception of inflationary inertia. Finally, market participants may have different assumptions about the reaction function of monetary policy.

16. As a result, Copom evaluated that the recent worsening in inertial components of inflation, amid the reopening of the service sector, could cause a further deterioration in inflation expectations, raising the costs for its future convergence. The Committee felt that it should once again underscore its unequivocal commitment to the pursuit of its inflation targets over the relevant horizon for monetary policy, guided by its baseline scenario as well as its assessment of the balance of risks.

17. Finally, Copom concluded that a quicker adjustment of monetary policy is the most appropriate strategy at this time to assure the convergence of inflation to its targets for 2022 and 2023.

#### **D) Monetary policy decision**

18. Taking into account the baseline scenario, the balance of risks, and the broad array of available information, Copom unanimously decided to increase the Selic rate by 1.00 p.p. to 5.25% p.a. The Committee judges that this decision reflects its baseline scenario for prospective inflation, a higher-than-usual variance in the balance of risks and is consistent with the convergence of inflation to its target over the relevant horizon for monetary policy, which includes 2022 and, to a lesser extent, 2023. The adjustment also reflects the Committee's perception that the recent deterioration of inertial components of inflation, in a moment of reopening of the service sector, could result in an additional deterioration of inflation expectations. The Committee understands that, at this moment, the strategy of a quicker monetary adjustment is the most appropriate to guarantee the anchoring of inflation expectations. Without compromising its fundamental objective of ensuring price stability, this decision also implies smoothing of economic fluctuations and fosters full employment.

19. At this moment, the Copom's baseline scenario and the balance of risks indicate as appropriate a tightening cycle of the policy rate to a level above the neutral.

20. For the next meeting, the Committee foresees another adjustment of the same magnitude. Copom emphasizes that its future policy steps could be adjusted to ensure the achievement of the inflation target and will depend on the evolution of economic activity, on the balance of risks, and on inflation expectations and projections for the relevant horizon for monetary policy.

21. The following members of the Committee voted for this decision: Roberto Oliveira Campos Neto (Governor), Carolina de Assis Barros, Fabio Kanczuk, Fernanda Magalhães Rumenos Guardado, João Manoel Pinho de Mello, Maurício Costa de Moura, Otávio Ribeiro Damaso, and Paulo Sérgio Neves de Souza.