250th

Minutes of the Meeting of the

Monetary Policy Committee — Copom

October 25-26, 2022

BANCO CENTRAL DO BRASIL

Date: October 25-26, 2022

Place: BCB Headquarters' meeting rooms on the 8th floor – Brasilia – DF – Brazil

Starting and ending times: October 25: 10:15 AM – 12:12 PM; 2:15 PM – 5:21 PM
October 26: 10:04 AM – 11:05 AM; 2:35 PM – 6:35 PM

In attendance:

Copom Members

Roberto de Oliveira Campos Neto – *Governor*
Bruno Serra Fernandes
Carolina de Assis Barros
Diogo Abry Guillen
Fernanda Magalhães Rumenos Guardado
Maurício Costa de Moura
Otávio Ribeiro Damaso
Paulo Sérgio Neves de Souza
Renato Dias de Brito Gomes

Department Heads in charge of technical presentations (attending on 10/25 and on the morning of 10/26):

Alan da Silva Andrade Mendes – *Department of Foreign Reserves*
André Minella – *Research Department (also present on the afternoon of 10/26)*
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 (attending on 10/25 and on the morning of 10/26):

Alexandre de Carvalho – *Head of the Office of Economic Advisory*
Cristiano de Oliveira Lopes Cozer – *General Counsel*
Edson Broxado de França Teixeira – *Head of the Deputy Governor for Supervision's Office*
Eduardo José Araújo Lima – *Head of the Deputy Governor for Economic Policy's Office*
Eduardo Urbanski Bueno – *Head of the Governor's Office*
Euler Pereira Gonçalves de Mello – *Deputy Head of the Research Department*
Gilneu Francisco Astolfi Vivan – *Head of the Financial System Monitoring Department*
Julio Cesar Costa Pinto – *Head of the Deputy Governor for Monetary Policy's Office*
Leonardo Martins Nogueira – *Executive Secretary*
Mauro Zanatta – *Press Office Advisor*
Olavo Lins Romano Pereira – *Deputy Head of the Department of International Affairs*
Pedro Henrique da Silva Castro – *Deputy Head of the Department of Economics*
Renato Baldini Junior – *Head of the Department of Statistics*
Ricardo Franco Moura – *Head of the Prudential and Foreign Exchange Regulation Department*

The Copom members 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 scenario[1]

1. The global environment remains adverse and volatile, with downward revisions on prospective global growth. The tightening of the financial conditions in major economies, the persistence of the war in Ukraine with its consequences on energy supply to Europe, and the continuation of the Covid-19 policy in China reinforce a prospect of a slowdown in global growth in the coming quarters.

2. The inflationary environment remains challenging. There is an incipient normalization in supply chains and an accommodation in the prices of major commodities in the recent period, which should lead to a moderation in global goods-related inflationary pressures. In turn, the low level of labor market slack in some economies, coupled with high current inflation and a high degree of diffusion, suggests that inflationary pressures on the services sector may last longer.

3. The process of normalization of monetary policy in advanced economies continues towards contractionary rates synchronized across countries, tightening financial conditions, impacting economic growth expectations, and raising the risk of abrupt repricing movements in the markets. The Committee noted a stronger market sensitivity to fiscal fundamentals, including in advanced economies. This greater sensitivity, concomitant with tightening financial conditions, requires more attention from developing economies. The Committee continues to monitor the risks related to the global slowdown and the increase in risk aversion in a highly pressured inflationary environment.

4. Turning to the Brazilian economy, the set of indicators released since the previous Copom meeting continues to signal growth, albeit at a more moderate rate. The labor market continues to recover, but at a slower pace than in previous months.

5. Despite the recent reduction, driven by items which are more volatile and affected by tax measures, consumer inflation remains high. The recent releases have been strongly influenced by the reduction in administered prices, due to both the decrease in taxes and, to a lesser extent, the drop in international fuel prices. In addition, items related to industrial goods, reflecting the more intense decrease in producer prices and the reduction of pressures in global value chains, also showed deceleration. However, the inflation of the components more sensitive to the economic cycle and the monetary policy, which present greater inflationary inertia, remain above the range compatible with meeting the inflation target. Inflation expectations for 2022, 2023, and 2024 collected by the Focus survey are around 5.6%, 4.9%, and 3.5%, respectively.

B) Scenarios and risk analysis

6. In the reference scenario, the interest rate path is extracted from the Focus survey, and the exchange rate starts at USD/BRL 5.25[2] and evolves according to the purchasing power parity (PPP). The Committee assumes that oil prices follow approximately the futures market curve for the following six months and then start increasing 2% per year onwards. Moreover, the energy flag is assumed to be "green" in December 2022, and "yellow" in December 2023 and 2024. In this scenario, Copom's inflation projections stand at 5.8% for 2022, 4.8% for 2023, and 2.9% for 2024. Inflation projections for administered prices are -3.9% for 2022, 9.4% for 2023, and 3.8% for 2024. The Committee decided again to emphasize the six-quarter-ahead horizon, which reflects the relevant horizon, mitigates the primary effects from the tax changes but incorporates their second-round effects. On this horizon, which refers to the second quarter of 2024, the 12-month inflation projection stands at 3.2%. The Committee

[1] Unless explicitly stated otherwise, this update takes into account changes that occurred since the September Copom meeting (249th meeting).
[2] Value obtained according to the usual procedure of rounding the average USD/BRL exchange rate observed on the five business days ending on the last day of the week before the Copom meeting.

judges that the uncertainty in its assumptions and projections is higher than usual.

7. The Committee still considers that the commitment and determination of central banks to reduce inflationary pressures and anchor expectations raise the risk of a more pronounced global slowdown. There has been an adjustment in the extent and speed of the monetary policy tightening cycle in some advanced countries, which has led to a further tightening of financial conditions.

8. The Committee noted a stronger market sensitivity to developments affecting the fiscal fundamentals, including in advanced economies. The combination of higher interest rates and sovereign debts at historically high levels, raises questions about the sustainability of public debt in several countries. Besides, the lower liquidity of the sovereign securities markets increases risk perception and demand monitoring.

9. Data on economic activity, which contribute to the assessment of the degree of slack, point to a more moderate pace of growth recently. On the one hand, the momentum of the reopening of the economy in the services sector and the fiscal stimuli are still driving consumption growth, although these impulses should slow down. On the other hand, the impact of monetary policy and its lags point to a reduction in the pace of economic activity, which tends to worsen in the coming quarters.

10. The Committee discussed the already noticeable impacts of monetary policy on credit and economic activity data. One can notice an impact in recent data regarding both the composition of new household credit operations and the moderate increase in the delinquency rate, partly related to the behavior of the real disposable income, which suggests some reduction. The Committee observed that an additional challenge for the proper assessment of the dynamics of activity at the margin is in the seasonal adjustment of the series, especially of the indicators with a shorter sample period, due to the pandemic period. Exercises show a high sensitivity of the signal and the magnitude of the seasonally adjusted results to small changes in the samples and methods used.

11. In the domestic scenario, Copom believes that the permanent increase in spending and the uncertainty about its trajectory from next year on may increase the country's risk premia and inflation expectations as they put pressure on aggregate demand and worsen the fiscal path expectations. The Committee reiterates that there are several channels by which fiscal policy may affect inflation, including its effect on activity, asset prices, degree of uncertainty in the economy, and inflation expectations.

12. The Committee emphasizes that risks to its scenarios remain in both directions. Among the upside risks for the inflationary scenario and inflation expectations, it should be emphasized (i) a greater persistence of global inflationary pressures; (ii) the uncertainty about the country's future fiscal framework and additional fiscal stimuli that support aggregate demand, partially incorporated in inflation expectations and asset prices; and (iii) an output gap tighter than the currently adopted by the Committee in its reference scenario, especially in the labor market. Among the downside risks, it should be noted (i) an additional reduction in the prices of international commodities measured in local currency; (ii) a greater than projected deceleration of global economic activity; and (iii) the continuity of tax cuts assumed to be reversed in 2023. The Committee assesses that the still uncertain and volatile current scenario requires serenity when evaluating risks.

C) Discussion about the conduct of monetary policy

13. Copom discussed the conduct of monetary policy, considering the set of projections evaluated, as well as the balance of risks for inflation.

14. The 12-month inflation projection for the second quarter of 2024, in the scenario using the interest rate trajectory extracted from the Focus survey, remains consistent

with the strategy of inflation convergence to around the target over the relevant horizon. The Committee decided again to emphasize the six-quarter-ahead horizon for its projections, and stresses that this decision is conditional on the temporary nature of the taxes. Moreover, the Committee continues to consider that inflation projection for 2024 is also around the target. This assessment reflects the lower-than-normal visibility of the forward-looking scenario, which increases the uncertainty of the point projections communicated by the Committee over longer horizons.

15. Copom anticipates that, if the alternative scenario of maintaining tax exemption on fuels in 2023 materializes, it will again emphasize usual horizons that include the first quarter of 2023. However, it assesses that there will be no relevant impacts on the conduct of monetary policy since the primary effects of such measures are already being disregarded.

16. Copom began by discussing the evolution of the broad array of data monitored, the projections, inflation expectations, and the balance of risks. Inflation projections showed a slight increase at longer horizons, reflecting upward revisions for inflation of market prices in the short term and a small increase in the projection for administered prices. The Committee assesses that the projections remain at values consistent with the strategy of reaching a level around the target over the relevant horizon. Inflation expectations from the Focus survey showed a more pronounced drop at shorter horizons but remains relatively stable for longer ones. Risks remain high, requiring continuous monitoring and serenity in their assessment. Regarding the degree of slack in the domestic economy, the Committee continues to monitor different metrics and strategies for the assessment of the output gap, as well as for current and prospective activity, and considers that there has been some decrease in the estimated slack since its latest update. Copom reinforces that its projection incorporates an increase in slack throughout the monetary policy horizon, as a result of the monetary adjustment undertaken in recent quarters. Finally, the Committee is following with special attention the evolution of services inflation, which depends on both inflationary inertia and the output gap, and whose trajectory will become clearer over time.

17. Copom chose to maintain the interest rate, reinforcing the need to evaluate, over time, the accumulated impacts to be observed of the intense and timely monetary policy cycle already undertaken. Therefore, the Committee members assessed that, given the data released, projections, inflation expectations, the balance of risks, and the lags of the effects of the monetary policy already in significantly contractionary territory, it was appropriate to maintain the interest rate at 13.75% p.a. The Committee reinforced that it is necessary to remain vigilant, assessing if the strategy of maintaining the Selic rate for a sufficiently long period will be enough to ensure the convergence of inflation.

18. The Committee emphasizes that it will persist until the disinflationary process consolidates and inflation expectations anchor around its targets. The Committee emphasizes that it will not hesitate to resume the tightening cycle if the disinflationary process does not proceed as expected.

D) Monetary policy decision

19. Considering the assessed scenarios, the balance of risks, and the broad array of available information, the Copom decided to maintain the Selic rate at 13.75% p.a. The Committee judges that this decision reflects the uncertainty around its scenarios for prospective inflation, an even higher-than-usual variance in the balance of risks, and is consistent with the strategy for inflation convergence to a level around its target throughout the relevant horizon for monetary policy, which includes 2023 and 2024. Without compromising its fundamental objective of ensuring price stability, this decision also implies smoothing of economic fluctuations and fosters full employment.

20. The Committee will remain vigilant, assessing if the strategy of maintaining the Selic rate for a sufficiently long period will be enough to ensure the convergence of inflation. The Committee emphasizes that it will persist until the disinflationary process consolidates and inflation expectations anchor around its targets. The Committee reinforces that future monetary policy steps can be adjusted and will not hesitate to resume the tightening cycle if the disinflationary process does not proceed as expected.

21. The following members of the Committee voted for this decision: Roberto de Oliveira Campos Neto (Governor), Bruno Serra Fernandes, Carolina de Assis Barros, Diogo Abry Guillen, Fernanda Magalhães Rumenos Guardado, Maurício Costa de Moura, Otávio Ribeiro Damaso, Paulo Sérgio Neves de Souza, and Renato Dias de Brito Gomes.