



LATIN AMERICA ECONOMICS UPDATE

BCB to continue to cut in 50bp steps

- **Brazil's central bank (BCB) cut the Selic rate by 50bp, to 12.25%, at yesterday's Copom meeting and signalled again that further similar reductions lie in store over the next few meetings. Even so, with strong wage growth set to keep inflation above target over the next 12-18 months and fiscal risks one again rearing their head, we think there is less scope for easing than most analysts currently anticipate.**
- The decision was widely predicted after being well signalled by Copom at its previous meeting in September and, similar to that decision, all Copom members were in favour. **The accompanying statement was little changed. Officials noted that the latest data had pointed to softer economic growth recently.** The BCB's economic activity indicator points to a q/q contraction in Q3. (See Chart 1.) Meanwhile, **October's mid-month inflation data** suggests that the recent rise in inflation has passed its peak. (See Chart 2.) **Copom assessed that the risks to the inflation outlook to be balanced.**
- Officials continued to emphasise the need for a contractionary monetary policy stance but retained their forward guidance for "further reductions [of the Selic] of the same magnitude". **For now, then, it looks like Copom will continue to lower rates in 50bp steps well into next year.**
- **Further ahead, as inflation proves more persistent than officials expect, Copom is likely to deliver less monetary easing than most currently anticipate.** While nominal **wage growth** has cooled, it remains strong (see Chart 3) and is likely to settle at rates that are consistent with core services inflation – which Copom is paying close attention to – of around 4% or so, above the BCB's target of 3.0% from next year.
- **Meanwhile, fiscal risks have reared their head again.** Last week, President Lula suggested that the government may no longer aim for a balanced primary budget as his government had previously pledged. That had initially weighed on the real, although the currency has since recouped its losses.
- **The upshot is that we expect the Selic to be cut to 9.50% by the end-2024 which is a little higher than most others currently anticipate.** (See Chart 4.) A key risk to our view stems from the shifting composition of Copom. Fernanda Guardado, among Copom's more hawkish members, alongside Mauricio Moura will soon depart and be replaced by Lula-nominees Paulo Picchetti and Rodrigo Teixeira. There's a clear risk that the new members prove to be more sympathetic to the president's desire for lower rates.

Chart 1: BCB Economic Activity Indicator & GDP

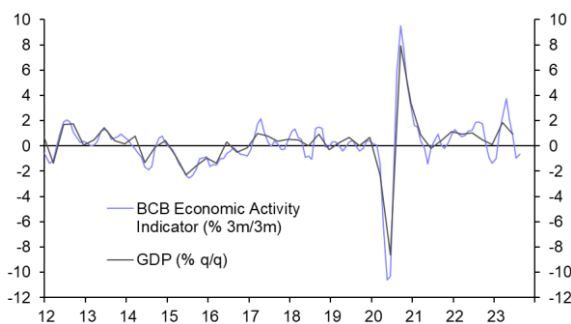


Chart 2: Consumer Prices (% y/y)

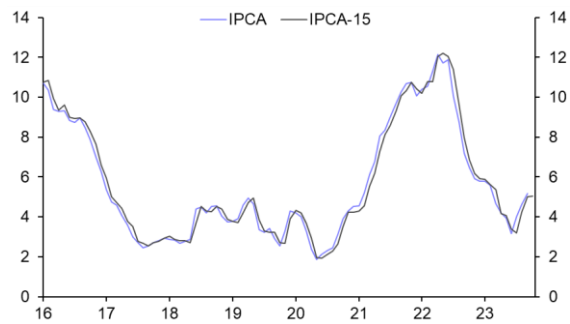


Chart 3: Average Nominal Wages

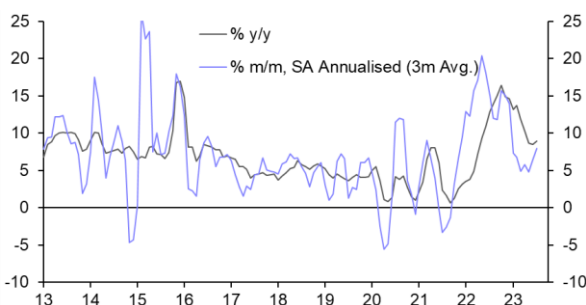
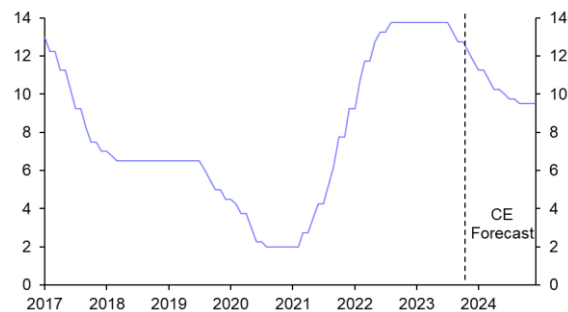


Chart 4: Selic Rate (%)



Sources: Refinitiv, BCB, Capital Economics



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