Santander
Macroeconomic Research

BRAZIL MACRO

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MONETARY POLICY PREVIEW

ARE WE THERE YET?

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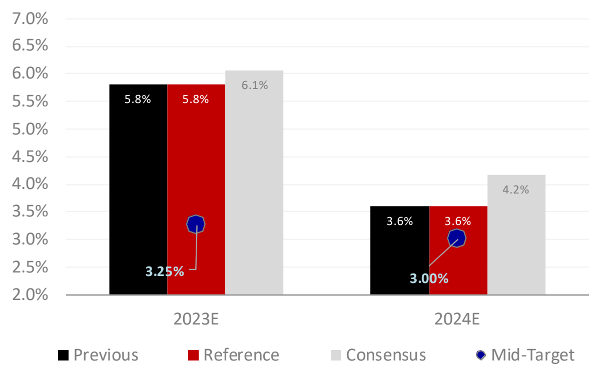
- The Copom is scheduled to announce its interest rate decision tomorrow (June 21, 2023). In line with consensus - as signaled by both analyst surveys and the yield curve pricing- we expect the Brazilian Central Bank (BCB) to maintain the Selic rate at 13.75%, a contractionary level. However, we expect the rate-announcement to be the least important part of tomorrow's meeting.
- The market focus is on the tone of the BCB's wording on the inflation outlook and risks, as well as the possible signals regarding the next policy steps. On one hand, we recognize that the conditions for monetary policy are starting to gradually change, as the tight BCB policy stance could be beginning to show its initial effects on the economy and on inflation. The market's constructive outlook about broad economic policy is also helping. Additionally, inflation expectations and underlying inflation figures are starting to reverse direction.
- In terms of the BCB inflation projections, our analysis based on the elasticities of key variables driving the BCB's forecasts suggest that the IPCA estimate for the reference scenario (i.e., assuming rate cuts starting in August) for 2024 could drop to 3.3%, from 3.6% in May's Copom. In our view, this will likely be seen as good progress for the BCB's inflation-fighting strategy, but we suspect that the authority will stop short of pre-signaling a rate cut for August. Two reasons for this: firstly, despite the narrowing gap between the BCB's IPCA projection and the mid-target, broad inflation expectations (i.e., both analysts' projections and premium-adjusted breakeven rates) for the medium and long term continue to run around % (i.e., significantly topping the 3% target), which we interpret as a still "uncomfortable level". Moreover, there is still uncertainty regarding decisions to be made by the CMN (Monetary Council) on the inflation targeting framework on June 29, 2023, and the subsequent effects on inflation expectations.
- There is also a significant gap between the BCB's inflation projections for market-set (i.e., non-regulated prices, the ones more sensitive to monetary policy) and the consensus estimates: in the last Copom, the BCB's official estimate for that group was 3.1% for 2024, whereas the consensus was 4.0% (and now is 3.9%). We believe that part of the mismatch has to do with the BCB's hypothesis for the level of real neutral interest rate, as the authority continues to estimate 4%. We and consensus estimate ~5%. A hypothetical incorporation of a higher estimate for the structural rate could make the gap between BCB projections and the target for 2024 to hold for a bit longer.
- In our view, despite constructive signals of late, the BCB remains concerned about de-anchored inflation expectations (still at ~4%) and the resilience in core services (still at ~6%). That, alongside lingering uncertainties (on the CPI target, new fiscal framework) may limit the BCB's softness in the communiqué. In other words, we believe the progress is still not enough for the BCB to change its strategy now, and so we expect the BCB to retain the current strategy (of holding rate) for the time being and maintain the message of "serenity and patience" to guarantee the inflation convergence for the medium term. We expect the Copom to signal that the next steps will be data dependent (especially on underlying inflation and inflation expectations).
- In our view, minimizing the probability of false starting in the easing cycle could have positive and lasting fruits for the (i) disinflation process, (ii) structural interest rate, and (iii) economy's long-term potential.

A LITTLE BACKGROUND ON PREVIOUS POLICY SIGNALS

In the 254th monetary policy meeting[1] of the BCB, held on May 2-3, the Copom maintained the Selic rate at 13.75%, as widely expected by the analysts and the yield curve. The BCB maintained the monetary policy signal that it “remains vigilant, assessing if the strategy of maintaining the Selic rate for a long period will be enough to ensure the convergence of inflation”. Referring to a more difficult stage of the disinflation process currently, the BCB once again signaled that “the current scenario demands patience and serenity in the conduct of monetary policy”.

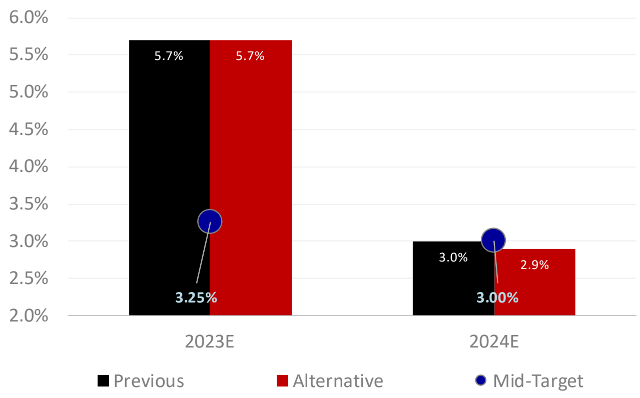
On the one hand, the BCB’s inflation models conveyed a message that, in the absence of major changes in key variables or BCB hypotheses influencing them, there was no room for Selic rate cuts. The numbers also reinforced, on the other hand, that the authority does not need to raise interest rates to achieve its objectives. The authority projected[2] IPCA at 3.6% for 2024 in a scenario with the rate cuts projected by economists, with convergence to mid target (3.0%) taking place in a counter-factual scenario of stable Selic rate all the way at 13.75%. Not a coincidence that the BCB downplayed the relevance of the claim that “it will not hesitate to resume the tightening cycle if the disinflationary process does not proceed as expected”, as the Copom made it clear that this was judged as a “less likely scenario.”

Figure 1. BCB’s Inflation Estimates (%, Reference)



Sources: Brazilian Central Bank, Santander.
Note: Assuming FX rate departing from USD/BRL 5.05, and then moving along with the PPP (purchasing power parity). Oil price following the futures curve for six months and stable in real terms in USD. Uses the consensus forecast for the future path of interest rate: 12.50% for YE2023 and 10.00% for YE2024.

Figure 2. BCB’s Inflation Estimates (%, Alternative)



Sources: Brazilian Central Bank, Santander.
Note: Assuming FX rate departing from USD/BRL 5.05, and then moving along with the PPP (purchasing power parity). Oil price following the futures curve for six months and stable in real terms in USD. Uses a path of stable interest rate at 13.75% for the entire horizon.

The balance of risks analysis of the statement basically maintained the same (upside and downside) elements, with some BCB emphasis on the uncertainty still present around “the final fiscal framework to be approved by Congress". The BCB also reaffirmed that monetary policy will focus on the “impacts on the expected paths of the public debt and of inflation expectations, and on risky assets”. As per the Brazilian economy, local activity data is still seen corroborating “the deceleration expected by Copom”, but the authority sees signs of resilience in the labor market. On inflation, the BCB avoided celebrations with the recent softening, indicating that headline and underlying inflation remain “above the range compatible with meeting the inflation target”.

In the Copom minutes[3], the BCB reiterated its commitment to the inflation target and reaffirmed its concern about the signs of rising expectations (still seen as partially related to discussions on the inflation

[1] **Santander Brazil Monetary Policy: “Copom Decision: *Same Tone, Same Strategy”*** – May 3, 2023 – Available on: https://bit.ly/Std-COPOM-may23.
[2] The simulations assumed USD/BRL at 5.05 and then evolving with the purchasing power parity (PPP) as well as oil price following the futures curve for the next six months and then stable in real terms in USD (i.e., up 2% annually subsequently). The scenarios assumed energy tariff flag "green" (previously "yellow") for both December 2023 and 2024. In the reference scenario, the BCB used a path of Selic rate cuts starting in September, reaching 12.50% for YE2023 and 10.00% for YE2024.
[3] **Santander Brazil Monetary Policy: “COPOM MINUTES: Lower Tail Risks in Fiscal Policy Do Not Change the BCB’s Inflation Outlook*”*** – May 9, 2023 – Available on: https://bit.ly/Std-COPOM-min-may23.

target) and the inertia of underlying inflation (still seen mostly as a by-product of excess demand in services). The BCB reaffirmed the principle of separation of instruments — with the monetary policy focused on fighting inflation and macroprudential measures seeking a proper functioning of financial and credit markets. The local credit slowdown was still seen as in line with BCB expectations, given the contractionary policy stance.

On the fiscal side, the BCB once again signaled that there was no mechanical relationship between the fiscal framework and monetary policy, given that the disinflationary effects of the former will need to be channeled through inflation expectations and financial conditions. The BCB recognizes that the government proposal for a new fiscal framework reduced the probability of more extreme scenarios for the debt trajectory but points out that there were no significant changes in economists' inflation expectations and, therefore, in the BCB's IPCA projections.

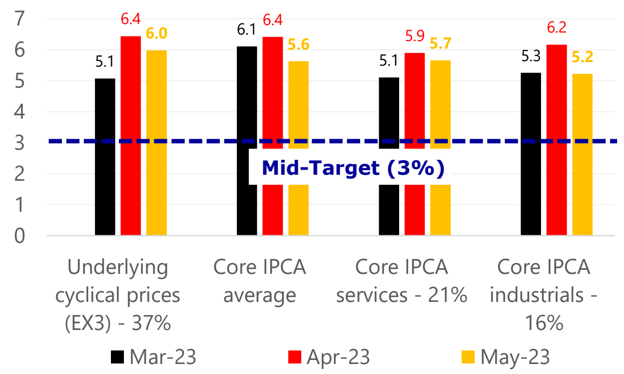
In the May Copom, the authority maintained the indication that the disinflation process is at the most difficult stage (given the spreading of pressures in services inflation), which requires a moderation in economic activity. The BCB also preached "serenity and patience" as it attempts to meet the target. The BCB indicated at that occasion that it would not get carried away if the expected temporary drop in year-on-year inflation in 2Q24 materializes. Overall, the last set of BCB communications in the last policy meetings gave us the impression that a change in the BCB strategy was premature at that point.

THE CONTEXT FOR THE JUNE MEETING

Since the May 2-3 Copom policy meeting[4], we recognize there has been progress on the inflation front, even when we filter out the influences of temporary effects, such as lower food costs, reductions in fuel prices, and tax cuts on auto sales (note: the latter is expected to impact CPI from June onwards). In fact, May's IPCA report not only showed headline inflation falling below the 4% threshold for the first time in more than two years, but more importantly it has pointed to a little easing in key underlying measures.

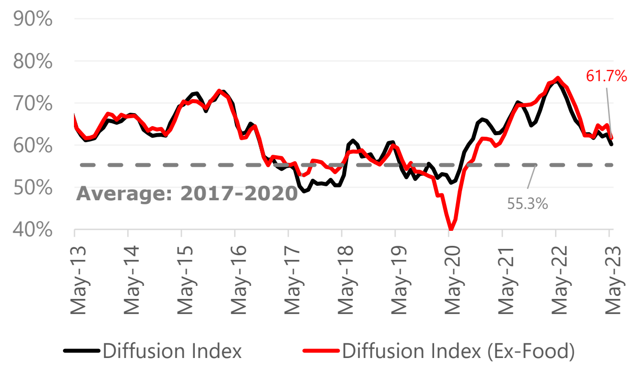
The most important core inflation gauge in our view — the EX3, the most closely correlated with economic activity and monetary policy cycles — is now running at a pace of around 6.0% QoQ-saar – according to our own seasonal adjustment. While its trend has indeed fallen from a clip of 6.4% in April, it continues to top the levels seen in March. Core services is showing a similar pattern – with its trend running at 5.7%, about 0.2 pp shy of April but still higher than in March. In fact, the easing in core inflation is more visible on core goods, whose trend slowed to 5.2% in May from 6.2% in April (Figure 1). That is a likely reflection of a slowing demand in goods markets alongside an important decline in prices at producer level. In any case, these numbers still stand way above the mid-point inflation target of 3% for the medium run.

Figure 3. Recent Trends in Core Inflation (% QoQ-saar)



Sources: IBGE, Brazilian Central, Bank, Santander.

Figure 4. IPCA Diffusion Indexes (3-month average)



Note: The diffusion index measures the percentage of IPCA subitems posting price increases.
Sources: IBGE, Brazilian Central, Bank, Santander.

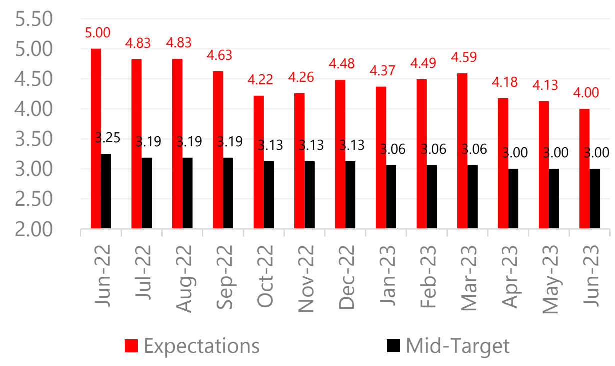
May inflation numbers also showed a decline in (our estimate for the seasonally adjusted) diffusion indexes – which measure the share of prices on the IPCA basket that are posting gains for the month. Still, as Figure 2 shows, it seems fair to say that the move is still incipient, as the (less volatile) 3-month average continues to

[4] **Santander Brazil Monetary Policy: "Copom: *Same Tone, Same Strategy"*** – May 3, 2023 – Available on: https://bit.ly/Std-COPOM-may23.

move around 61-62%, more than one standard deviation above the average of low-inflation years (i.e., ~55% for 2017 to 2019).

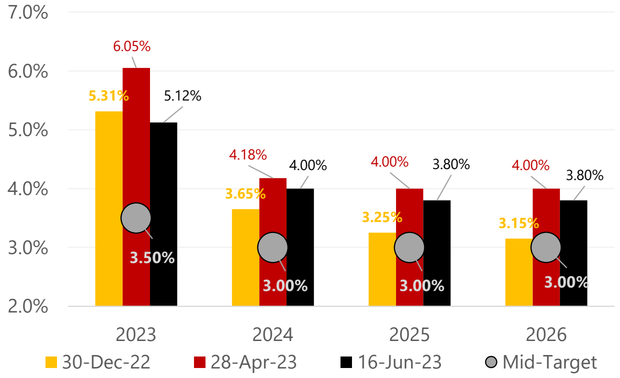
On the expectations front, both analysts' forecasts (Focus) and breakeven inflation rates (BEIRs) have declined for nearly all horizons since the last Copom. In terms of forecasts, there was a broad-based decline in the Focus survey for all horizons (2023 to 2027). For the short term, median IPCA forecast for 2023 slumped 93bps to 5.12%; for the medium term, we calculate that the 18-month forward estimate (which for now coincides with the policy horizon of YE2024) slid by 18bps to 4.00%. For the long term, the median IPCA projections fell ~20bps to 3.8% both for 2025 and 2026. The numbers still top the 3% medium-run target.

Figure 5. Calendar-Adjusted IPCA Estimates, Target *(18 months ahead)*



Sources: Brazilian Central Bank, Santander.
Note 1: IPCA expectations and target adjusted for the weight of each calendar-year as a policy horizon. For 2Q23, this means YE2024.
Note 2: Figures for the end of month. For June 2023 up to the 16th.

Figure 6. Median IPCA Inflation Expectations *(% annual)*



Sources: Brazilian Central Bank, Santander.
Note 1: As of the most recent BCB Focus report: June 19, 2023.

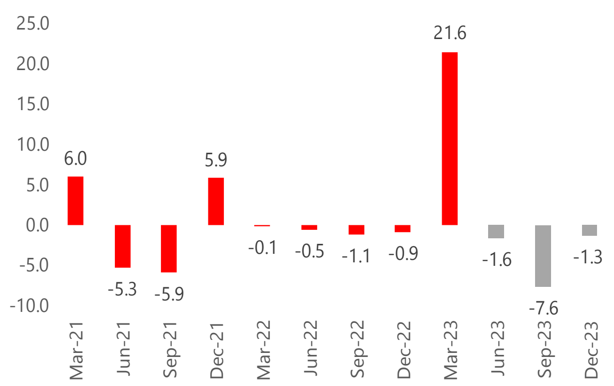
Breakeven inflation rates – naturally dependent on asset price swings, whose movements are usually more volatile than analysts forecast – fell way more aggressively: ~120bps for horizons up to 2 years and ~50 to 70bps for longer horizons (5 to 10 years). For the shorter horizons, BEIRs stand around 4%, with longer horizons showing implicit inflation rates in local bonds near 5.5%. Despite the decline, premium-adjusted[5] BEIRs still point to broad market expectations of inflation running around 4.0-4.5%, significantly above the mid-target (3%).

These developments likely mirror the continued signs of softening in goods prices, as the pressures in commodity prices fade. We estimate that materials costs in BRL are down ~20% trend-wise from their peak of mid-2022. When it comes to CPI forecasts for the longer term, part of the improving mood is based on expectations that the 3% mid-target for the long term could be maintained at the June 29 meeting of the CMN (Monetary Council). Still, services inflation remain under pressure and seems to prompt little relief for the time being.

Economic activity numbers continued to generate mixed feelings since the last Copom meeting, in our view. However, in general, the latest set of reports for 1Q23 and early 2Q23 continue to point to a gradual loss of steam, especially in the most cyclical sectors, despite some resilience still seen in the labor market. Although the 1Q23 GDP headline[6] has surprised on the downside – and led to massive upward revisions in economists' forecasts for FY2023 to just above 2% (from 1% previously) – the result was led by a whopping (but unfortunately one-off) increase in agriculture GDP, which primary production accounts for ~10% of Brazil's total output. In fact, the composition of the 1Q23 GDP was not very sanguine, as it showed the first quarterly sequential contraction in domestic demand since 2Q21.

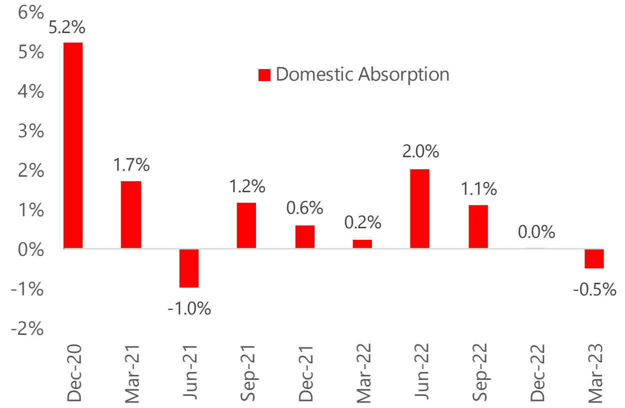
[5] We calculate that the historical premium of breakeven inflation rates (vis-à-vis economists' inflation forecasts) is usually ~50bps for horizons up to 2 years, about 75bps for 5 years and ~100bps for 10 years.
[6] **Santander Brazil Activity: "Agricultural Sector Leads Strong 1Q23 GDP Growth"** – June 1, 2023 – Available on: https://bit.ly/Std-GDP-1Q23

Figure 7. Agriculture GDP: Histrory, Forecasts (% QoQ-saar, quarterly series)



Sources: IBGE, Santander. Note: Santander forecasts.

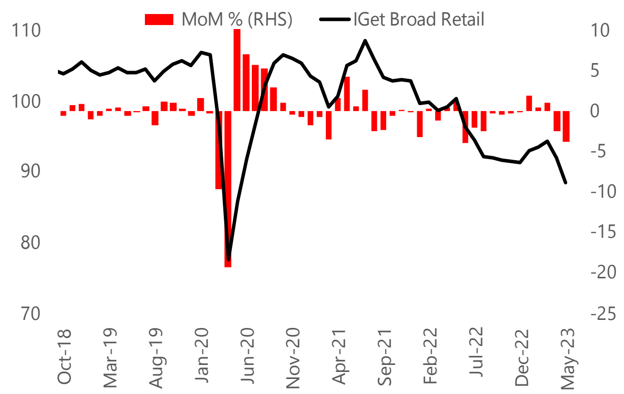
Figure 8. Evolution of Domestic Demand (ex-inventories, % QoQ-saar, quarterly series)



Sources: IBGE, Santander. Note: Santander estimates.

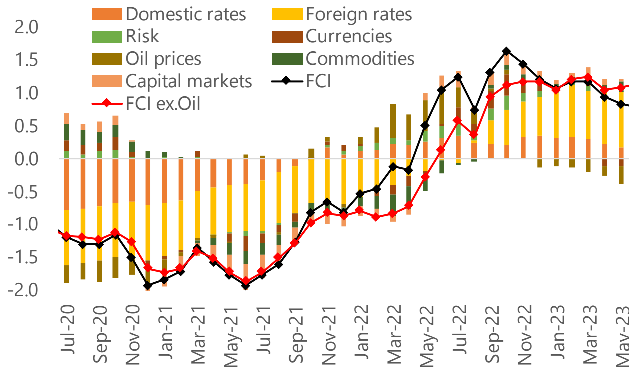
The early activity numbers for the 2Q23 have not been very encouraging either[7]. Despite the gain in the IBC-Br for (the BCB's monthly GDP proxy) for April, most of the key high-frequency indicators point to a continued deceleration, especially in the tertiary sector, which had services as a key driver for growth in previous quarters. Our proprietary activity indicators from the IGet[8] family also indicate a continued loss of steam in both retail and services for May[9]. The numbers suggest that the good reading of the IBC-Br early in 2Q23 could reflect short-term influences from agriculture and maybe some difficulties with the seasonal adjustment[10]. Moreover, credit activity has also been on the backfoot (with latest data regarding April), despite the lack of any evidence whatsoever of a major (dysfunctional) credit crunch: in our view[11], both bank lending and capital market issuance are seeing a deceleration of credit on the back of high interest rates, high consumer indebtedness and high risk premium (the latter reflecting increasing delinquency both for households and corporates).

Figure 9. IGet Broad Retail Index



Sources: Santander.

Figure 10. Santander's Financial Conditions Index



Sources: Santander.

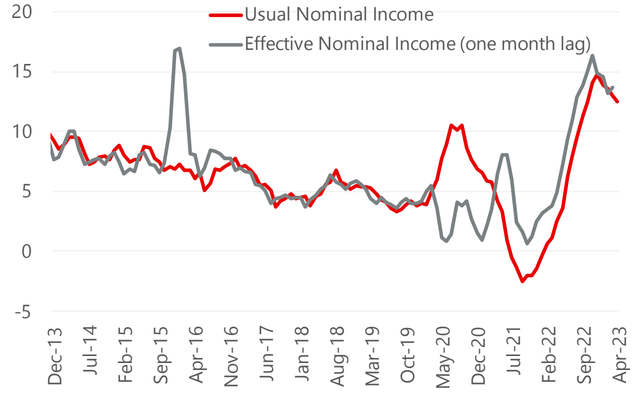
All in all, both the weak details of 1Q23 and the fading momentum into 2Q23 could help explain the decline in median GDP forecasts for FY2024, reaching 1.2%, down 0.2 pp since the lats Copom meeting. Looking ahead, the BCB's scenario of a slowing economy tends to materialize mainly on the back of a contractionary monetary

[7] **Santander Brazil - Macro Compass: "Another Week for Bulls; Watching BCB's Signs"** – June 16, 2023 – Available on: https://bit.ly/Std-macrocomp-061623
[8] **Santander Brazil IGET RETAIL**: "Dados consolidados de maio apontam nova contração da atividade varejista ampliada" - 7 de junho de 2023 - disponível em: https://bit.ly/Std-IGET-mai23 (Portuguese only)
[9] **Santander Brazil IGET SERVICES**: "Serviços em queda no consolidado de maio" - 7 de junho de 2023 - Disponível em https://bit.ly/Std-IGETser-mai23 (Portuguese only)
[10] The hypothesis is that recent revisions in IBGE's series for short-term surveys (such as industrial production, retail sales and services revenues) could have impacted the estimates of parameters in the seasonal adjustment procedures for some key activity indicators.
[11] **Santander Brazil Credit: "Household and Corporate Default Rate Continue to Rise"** – May 30, 2023 – Available on: https://bit.ly/Std-credit-may23

policy and a consequently tight financial conditions (despite some easing of late generated by this rally in Brazilian asset prices) over the last few months.

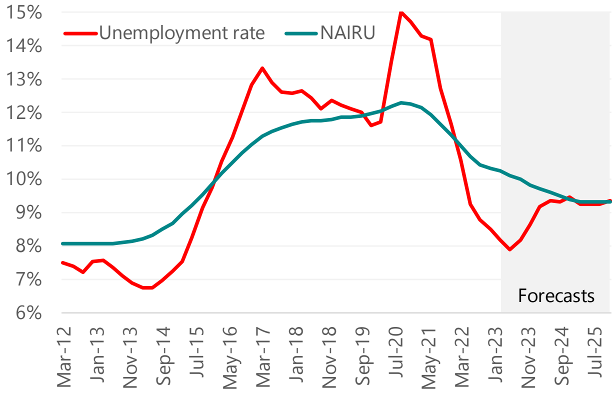
Despite the notorious deceleration trend, there are still some positive drivers (other than farm output) providing a little support for the economy. Although part of the low unemployment rate of late can be associated with a decline participation rate (i.e., lower labor supply), the trend payroll growth (as signaled by CAGED's formal employment data) has been running just below 200k per month, topping the neutral level for the jobless rate (~100k). This signal still positive labor demand. We estimate the unemployment rate – currently running just above 8%, seasonally adjusted – stands below the NAIRU (the long-term, inflation-neutral level) of ~10%, according to our calculations.

Figure 11. Nominal Average Income (% YoY)



Sources: IBGE, Santander.
Note: Monthly data.

Figure 12. Joblessness and Structural Unemployment

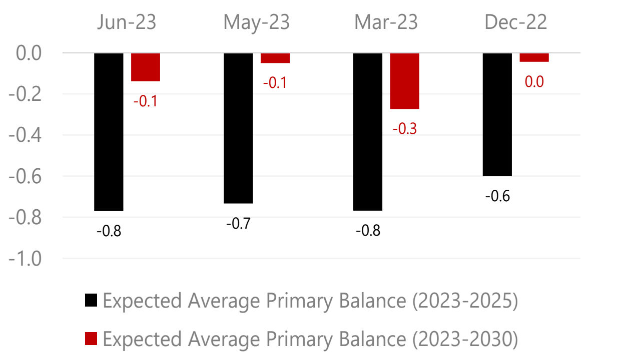


Sources: IBGE, Santander.
Note: Quarterly data.

With low unemployment, be it for the good (labor demand) or the bad (labor supply) reasons, this is not a coincidence that nominal average wages continue to grow at a pace of 12-13% YoY, meaning a potential increase in unit labor costs (given the economy's low productivity growth of late). **In our view, the still fast growth in wages is a likely signal that the economy has limited (if any at all) degree of slack, especially in the job market[12] and in the (labor-intensive) services sector.**

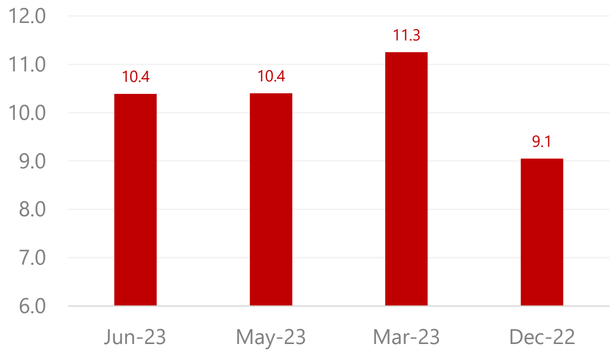
Since the last Copom meeting, we have also witnessed financial market's apparently supportive view of the new fiscal framework — which is now in line for final approval in the Senate. The advance of the new legislation in the Lower House could also have played a role in the substantial improvement in Brazilian asset prices and in the corrosion of premia (in both FX and fixed income), leading to better financial conditions since the last meeting. Yet we believe the rally in Brazilian assets is also related to a larger global appetite for risk assets, given investors' perception of an increased probability that the Fed is near the end of its tightening cycle.

Figure 13. Expectations for Primary Balance (% GDP)



Sources: Brazilian Central Bank, Santander.
Note: Based on the median forecasts for the public sector's primary balance, as per the Focus survey of June 19, 2023.

Figure 14. Expected Increase in Govt Debt (% GDP)



Sources: Brazilian Central Bank, Santander.
Note: Based on the median forecasts for gross general government debt from 2023 to 2030, as per the Focus survey of June 19, 2023.

[12] **Santander Brazil Activity: "Positive Surprises for Labor Market in April"** – May 31, 2023 – Available on: https://bit.ly/Std-labor-053123

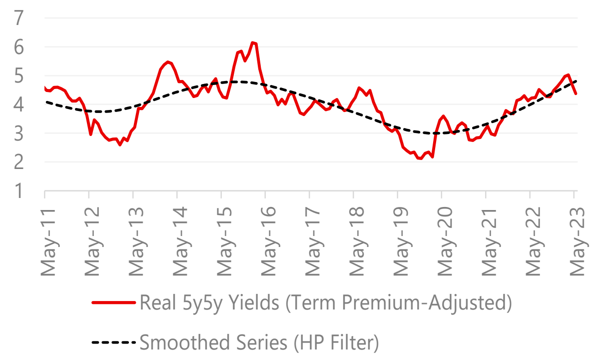
In fact, we note important challenges in the implementation of the legislation to achieve the bold objectives (such as eliminating the primary deficit next year)[13]. Moreover, economists' forecasts for both the public sector's primary fiscal balance and the general government's gross debt to GDP ratio have not changed at all in the weeks following the approval of the legislation at the Lower House. In fact, economists continue to project primary deficits of ~1% of GDP for the period of 2023-2025, as well as a zero-ish average result for the period spanning 2023 to 2030 (meaning expectations of a primary surplus, but only as we head closer to the end of the decade). Analysts also continue to expect the debt ratio to increase by a little more than 10 pp of GDP until 2030, same as in previous weeks.

WHAT TO EXPECT FROM THE MEETING AND THE SIGNALS FOR THE FUTURE STEPS?

In terms of the BCB inflation projections, our analysis based on the elasticities of key variables driving the BCB's forecasts suggests that the IPCA estimate for the reference scenario could drop to 4.5%[14] (from 5.8%) for 2023 and to 3.3% (from 3.6%) for 2024 – the key policy horizon. In our view, this will likely be seen as a good progress in the inflation-fighting by the BCB, but we suspect that the authority will still fall short of pre-signaling a rate cut for August. Two set of reasons for this: firstly, despite the narrowing gap between the BCB's IPCA projection and the mid-target, broad inflation expectations (i.e., both analysts' projections and breakeven rates) continue to run around 4% (i.e., still significantly topping the 3% target), which we interpret as a still "uncomfortable level". Moreover, there is still the uncertainty element regarding the decisions to be made by the CMN (Monetary Council) on the inflation targeting framework on June 29, 2023, and the subsequent effects on expectations.

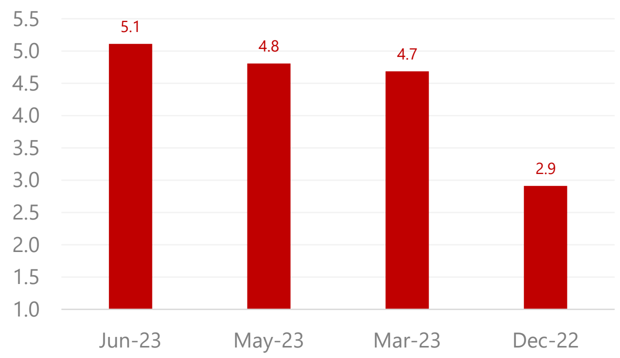
Second, it is important to bear in mind the significant gap between the BCB's inflation projections for market-set (i.e., non-regulated prices, the ones more sensitive to monetary policy) and the consensus estimates: in the last Copom, the official BCB's estimate for that group was 3.1% for 2024, whereas the consensus was 4.0%[15]. We believe that part of the mismatch has to do with the BCB's (possibly outdated) hypothesis for the level of real neutral interest rate, as the authority continues to use an estimate of 4%. We and the consensus of economists now estimate a figure ~5%.

Figure 15. Santander's Real Neutra Rate Proxy



Sources: Santander.

Figure 16. Implicit Consensus for Real Neutral Rate



Sources: Santander.
Note: As of the most recent BCB Focus report: June 19, 2023.

The debate of structural interest rate has apparently been a growing concern (or point of interest) by the technical staff of the BCB. And an incorporation of a 5% assumption for the structural rate could make the gap between BCB projections and the target for 2024 to hold for a bit longer. According to the last Copom minutes, some members believed in the last meeting that "a scenario marked by a possible rise in neutral interest rates in major economies, resilience in Brazilian activity, and a slow disinflationary process could be compatible with a higher measure of neutral rate than that assumed by the Committee". In their view, this would imply "a lower contractionary impact than that implicit in the Copom's scenarios." For now, however, the majority " judged that this interpretation still seems premature and needs further corroboration by data."

[13] **Santander Brazil Fiscal: "Chartbook: Without Major Changes, Challenges Remain Ahead"** – May 12, 2023 – Available on: https://bit.ly/Std-chart-fiscal-may23
[14] That is the numbers indicated by BCB officials in a recent public appearance.
[15] As of June 16, 2023, the consensus for unregulated prices dropped a bit to 3.9% (refer to the BCB's Focus survey among professional forecasters at https://www.bcb.gov.br/en/publications/focusmarketreadout).

In any case, we recognize that the conditions for monetary policy are starting to change, albeit gradually, as the tight BCB policy stance could be beginning to show its initial effects on the economy and on inflation. The market's constructive outlook about broad economic policy is also helping. While we expect these elements to slightly soften the Copom's statement next week (June 20-21), we believe the BCB could refrain from signaling immediate rate cuts, leaving its next steps more data dependent. Step by step, these events are eliminating the possibility of alternative scenarios for the short to medium term, taking the BCB closer to an inflexion point after holding the interest rate at the tight level of 13.75% for six policy meetings (i.e., ~9 months). In that sense, the mentions to a scenario of rate hikes could well drop out of the communiqué.

In recent speeches, BCB officials have conveyed a message that they see monetary tightening gradually achieving the desired effects, explicitly mentioning that an easing cycle might be ahead. However, the BCB is naturally trying to avoid mentioning a time frame, as apparently the authority still sees the progress so far as insufficient to start cutting rates now (the BCB's comparison of current conditions with previous easing cycles illustrates why).

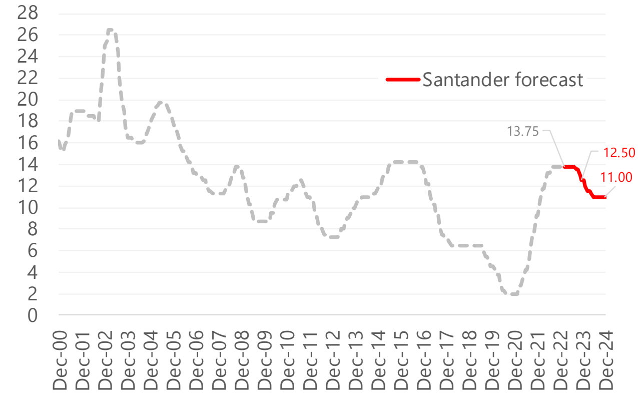
In our view, the BCB remains concerned about de-anchored inflation expectations (still at ~4%) and the resilience in core services (still at ~6%), and that, alongside lingering uncertainties (about the CPI target, new fiscal framework), will likely limit the BCB's dovishness in the communiqué. In our view, the progress is still not enough for the BCB to change its strategy now. Thus, we expect the BCB to retain the current strategy (of holding rate) for now and maintain the message of "serenity and patience" to guarantee the inflation convergence for the medium term. We expect the Copom to signal that the next steps will be data dependent (especially on underlying inflation and inflation expectations).

In our view, minimizing the probability of false starting in the easing cycle can have positive and lasting fruits for the disinflation process, for the structural interest rate and the economy's long-term potential.

We recently brought forward our projection for the beginning of the easing cycle and now expect an initial 25-bp cut in September (from November). This means a Selic rate projection of 12.50% for YE2023 (previously 13.00%). Considering the lingering risks from an overheated economy and the execution of the new budget framework, we see a cautious BCB and maintain our Selic rate projection at 11% for YE2024.

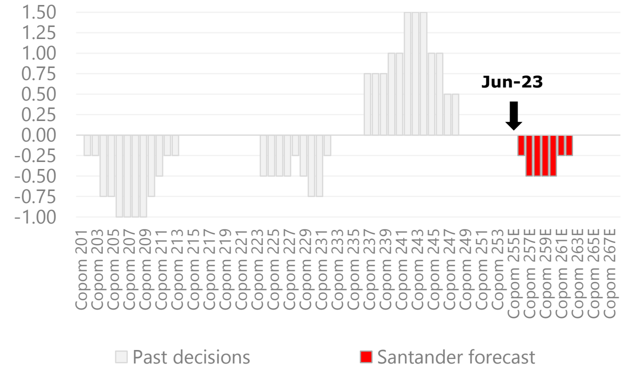
Refer to a summary of the Copom dataset and the following graphs.

Figure 17. Santander Selic Forecast (% pa)



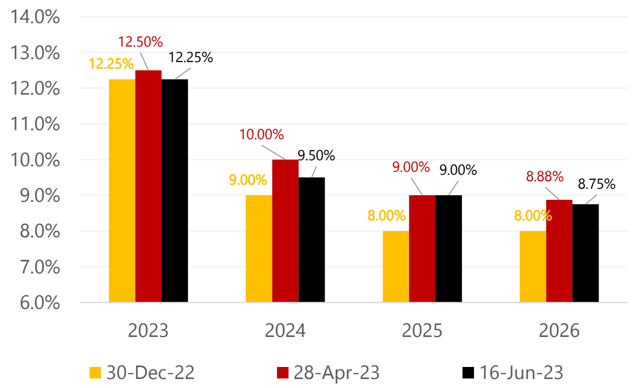
Sources: Brazilian Central Bank, Santander.

Figure 18. Historical, Expected BCB Moves (% pp)



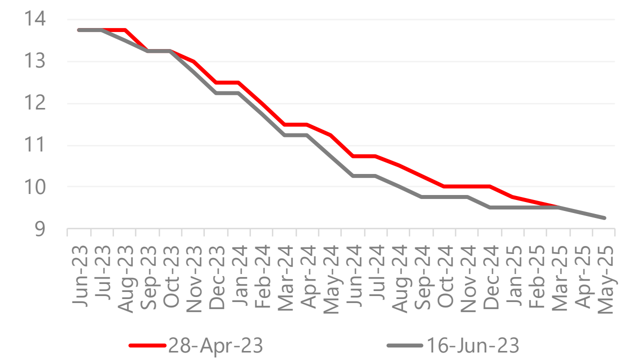
Sources: Brazilian Central Bank, Santander.

Figure 19. Median Selic Rate Expectations *(% annual)*



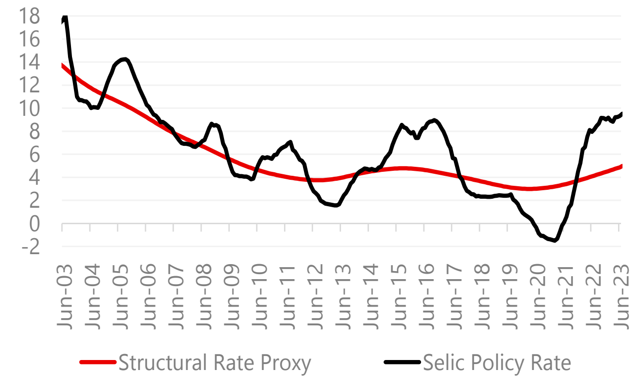
Sources: Brazilian Central Bank, Santander.
Note: As of the most recent BCB Focus report: June 19, 2023.

Figure 20. Median Selic Rate Expectations *(% annual, monthly path)*



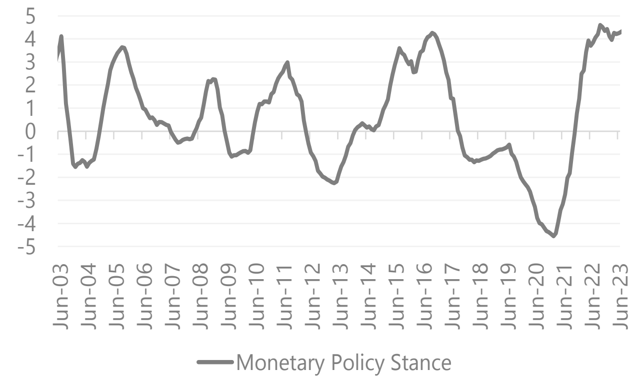
Sources: Brazilian Central Bank, Bloomberg, Santander.
Note: As of the most recent BCB Focus report: June 19, 2023.

Figure 21. Real Rates: Short Term vs. Long Term *(monthly average, % annual)*



Sources: Brazilian Central Bank, Bloomberg, Santander.
Note 1: The neutral rate proxy is based on long-term real yields (5y5y forwards) adjusted by a constant historical term premium of 150bps.
Note 2: Average for June 2023 up to the 16th.

Figure 22. Estimated Monetary Policy Stance *(gap between long and short-term real rates)*



Sources: Brazilian Central Bank, Bloomberg, Santander.
Note 1: To calculate the policy stimulus, we subtract from the real policy rate the real level of neutral rate proxy (see graph on the left side).
Note 2: Average for June 2023 up to the 16th.

Figure 23. Proxy for the Copom Dataset, Part 1

ECONOMIC TOPIC	LATEST DATA		THIS MEETING	LAST MEETING	SECOND LAST
Key Variables	*When?*		*Jun-23*	*May-23*	*Mar-23*
INFLATION					
Forecasts (% p.a.) - BCB's Focus report					
Calendar-Weighted Forecast (~18 months)	16-Jun-23	↓	4.00	4.18	4.57
Calendar-Weighted Target (~18 months)	16-Jun-23	→	3.00	3.00	3.06
Calendar-Weighted Expectations Gap	16-Jun-23	↓	1.00	1.18	1.51
Forecast for a year ahead (12 months)	16-Jun-23	↓	4.18	5.23	5.44
Forecast for 2023 - target: 3.25%	16-Jun-23	↓	5.12	6.05	5.95
Forecast for 2024 - target: 3.00%	16-Jun-23	↓	4.00	4.18	4.11
Forecast for 2025 - target: 3.00%	16-Jun-23	↓	3.80	4.00	3.90
Forecast for 2026 - target: ???	16-Jun-23	↓	3.80	4.00	4.00
Forecast for 2027 - target: ???	16-Jun-23	↓	3.70	4.00	4.00
Breakeven inflation rates (% p.a.)					
1-year	16-Jun-23	↓	3.79	5.02	6.10
18-month	16-Jun-23	↓	4.14	5.35	5.92
2-year	16-Jun-23	↓	4.36	5.58	6.01
5-year	16-Jun-23	↓	5.23	5.93	6.58
10-year	16-Jun-23	↓	5.57	6.03	6.69
Actual CPI data					
Headline (% YoY)	May-23	↓	3.9	4.2	4.7
Headline (% QoQ, saar)	May-23	↓	6.7	7.6	7.8
Core IPCA EX3 (% YoY)	May-23	↓	8.0	8.7	9.1
Core IPCA EX3 (% QoQ, saar)	May-23	↓	6.0	6.4	5.1
Core IPCA Services (% YoY)	May-23	↓	7.1	7.5	7.8
Core IPCA Services (% QoQ, saar)	May-23	↓	5.7	5.9	5.1
New cores average (% YoY)	May-23	↓	9.2	10.2	10.9
New cores average (% QoQ, saar)	May-23	↓	5.2	6.2	5.3
Diffusion index (sa, 3m)	May-23	→	0.0%	0.0%	0.0%
Diffusion index ex-food (sa, 3m)	May-23	→	0.0%	0.0%	0.0%
MONETARY POLICY					
Selic rate (% p.a.)					
Current level	16-Jun-23	→	13.75	13.75	13.75
Forecast for 2023	16-Jun-23	↓	12.25	12.50	12.75
Forecast for 2024	16-Jun-23	↓	9.50	10.00	10.00
Forecast for 2025	16-Jun-23	→	9.00	9.00	9.00
Forecast for 2026	16-Jun-23	↓	8.75	8.88	9.00
Forecast for 2027	16-Jun-23	→	9.00	9.00	8.88
Yield curve (% p.a.)					
1-year OIS swaps (pré-DI)	16-Jun-23	↓	12.0	12.7	12.7
2-year OIS swaps (pré-DI)	16-Jun-23	↓	10.8	11.7	12.0
Ex-ante real interest rate (% p.a.)					
1-year (OIS swaps vs. inflation forecast)	16-Jun-23	↑	7.5	7.1	6.9
FISCAL POLICY					
Primary Fiscal Balance (% GDP)					
Actual level (12-month rolling)	Apr-23	↓	0.6	0.7	0.9
Forecast for 2023	16-Jun-23	↓	-1.0	-1.0	-1.0
Forecast for 2024	16-Jun-23	→	-0.8	-0.8	-0.8
Forecast for 2025	16-Jun-23	↓	-0.5	-0.4	-0.5
Forecast for 2026	16-Jun-23	↓	-0.3	-0.2	-0.2
Forecast for 2030	16-Jun-23	→	0.8	0.8	0.0
Gross General Government Debt (% GDP)					
Actual level	Apr-23	↑	73.0	73.0	72.6
Forecast for 2023	16-Jun-23	↓	76.5	77.1	77.8
Forecast for 2024	16-Jun-23	↓	79.1	80.3	80.9
Forecast for 2025	16-Jun-23	↓	82.0	82.1	82.2
Forecast for 2026	16-Jun-23	↓	83.1	83.3	84.2
Forecast for 2030	16-Jun-23	↓	86.9	87.5	89.0

Sources: IBGE, FGV, Brazilian Central Bank, Anbima, Bloomberg, Santander.

Last update: June 19, 2023.

Figure 24. Proxy for the Copom Dataset, Part 2

ECONOMIC TOPIC	LATEST DATA		THIS MEETING	LAST MEETING	SECOND LAST
Key Variables	*When?*		*Apr-23*	*Mar-23*	*Feb-23*
REAL ACTIVITY					
GDP forecasts (% p.a.) - BCB's Focus report					
Forecast for 2023	16-Jun-23	↑	2.14	1.00	0.88
Forecast for 2024	16-Jun-23	↓	1.20	1.41	1.47
Forecast for 2025	16-Jun-23	→	1.80	1.80	1.70
Forecast for 2026	16-Jun-23	↑	1.99	1.80	1.80
Forecast for 2027	16-Jun-23	↑	1.99	1.83	1.95
Actual activity data					
IBC-Br (% QoQ, saar)	Apr-23	↑	14.6	10.4	4.8
Industrial production (% QoQ, saar)	Apr-23	↑	0.3	-0.2	1.1
Broad retail sales (% QoQ, saar)	Apr-23	↑	19.9	15.7	7.7
Services volume (% QoQ, saar)	Apr-23	↑	-1.0	-2.7	2.3
Unemployment rate (% 3m, SA)	Apr-23	↓	8.1	8.2	8.3
Real wage bill (% YoY, 3m)	Apr-23	↓	9.6	10.8	11.4
Real average wage (% YoY, 3m)	Apr-23	↑	7.4	7.3	7.5
Nominal average wage (% YoY, 3m)	Apr-23	↓	12.5	13.0	13.6
Caged payrolls (thousands, SA, 3m)	Apr-23	↑	194	179	106
Economic confidence (2011=100)	May-23	↑	85.5	84.6	84.7
EXTERNAL SECTOR					
FX rate (USD/BRL)					
Current level	16-Jun-23	↓	4.82	4.99	5.24
Actual: 5-day average (previous week)	16-Jun-23	↓	4.84	5.02	5.26
USD/BRL (to be) used in simulations	**16-Jun-23**	↓	**4.85**	**5.05**	**5.25**
Forecast for 2023	16-Jun-23	↓	5.00	5.20	5.25
Forecast for 2024	16-Jun-23	↓	5.10	5.25	5.30
Forecast for 2025	16-Jun-23	↓	5.18	5.30	5.30
Forecast for 2026	16-Jun-23	↓	5.25	5.32	5.40
Forecast for 2027	16-Jun-23	↓	5.25	5.39	5.40
Current account balance (USD Billions, 12m)					
Current level (12-month rolling)	Apr-23	↓	-54.2	-52.4	-55.6
Forecast for 2023	16-Jun-23	↑	-45.3	-48.0	-50.0
Forecast for 2024	16-Jun-23	↑	-51.0	-52.8	-50.7
Forecast for 2025	16-Jun-23	↑	-50.3	-51.2	-48.6
Forecast for 2026	16-Jun-23	↑	-50.0	-51.0	-46.0
Forecast for 2027	16-Jun-23	↓	-59.5	-55.0	-55.0
ASSET PRICES					
Santander Brasil's financial conditions index*	**Jun-23**	↓	**0.66**	**0.84**	**1.18**
IC-Br (% YoY)	May-23	↓	-20.1	-13.4	-14.0
CRB Commodity Index (Futures, USD terms)	16-Jun-23	↑	271	257	259
CRB Commodity Index (Futures, BRL terms)	16-Jun-23	↑	1,307	1,286	1,362
CRB Commodities in BRL: 50-day average	16-Jun-23	↓	1,300	1,359	1,391
Brent Oil Price (USD bbl) / 1st Active Future	16-Jun-23	↑	77	72	76
Brazil 5-year CDS (basis-points)	16-Jun-23	↓	184	223	247
Ibovespa stock index (points)	16-Jun-23	↑	118,758	101,797	100,221
DI Jan-24 (% p.a.) / Futures	16-Jun-23	↓	13.02	13.24	13.02
DI Jan-25 (% p.a.) / Futures	16-Jun-23	↓	11.13	11.89	12.05
DI Jan-26 (% p.a.) / Futures	16-Jun-23	↓	10.50	11.58	12.09
NTN-F 2029 (% p.a.) / Pre-Fixed Rate	16-Jun-23	↓	10.99	11.98	12.78
NTN-F 2033 (% p.a.) / Pre-Fixed Rate	16-Jun-23	↓	11.18	12.13	13.05
NTN-B 2045 (% p.a.) / Inflation-Linked	16-Jun-23	↓	5.60	5.98	6.35
NTN-B 2060 (% p.a.) / Inflation-Linked	16-Jun-23	↓	5.60	5.99	6.34

Sources: IBGE, FGV, Brazilian Central Bank, Anbima, Bloomberg, Santander.

Last update: June 19, 2023.

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