Inflation Report

September 26th, 2024

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BCB's Deputy Governor for Economic Policy

Reference scenario

Reference scenario

External scenario

- The external scenario remains challenging, due to the inflection point of the economic cycle in the U.S., posing questions about the pace of economic deceleration, disinflation, and consequently, about the Fed's monetary policy stance.
- The central banks of major economies remain committed to bringing inflation back to its targets in a context characterized by labor market pressures.
- Copom assess that the external scenario, also marked by less synchronized monetary policy cycles across countries, continues to require caution from emerging market economies.

Economic activity

- Regarding the domestic scenario, the set of indicators on economic activity and labor market has exhibited more strength than expected by Copom, which led to a reassessment regarding the output gap as being positive.

Inflation

- Headline inflation measured by the IPCA as well as various measures of underlying inflation are above the inflation target in recent releases.
- Inflation expectations for 2024 and 2025 calculated by the Focus survey are around 4.4% and 4.0%, respectively.
- Copom's inflation projection for 2026Q1, the current relevant monetary policy horizon, stands at 3.5% in the reference scenario (4.3% for 2024 and 3.7% for 2025).

INFLATION REPORT (IR)

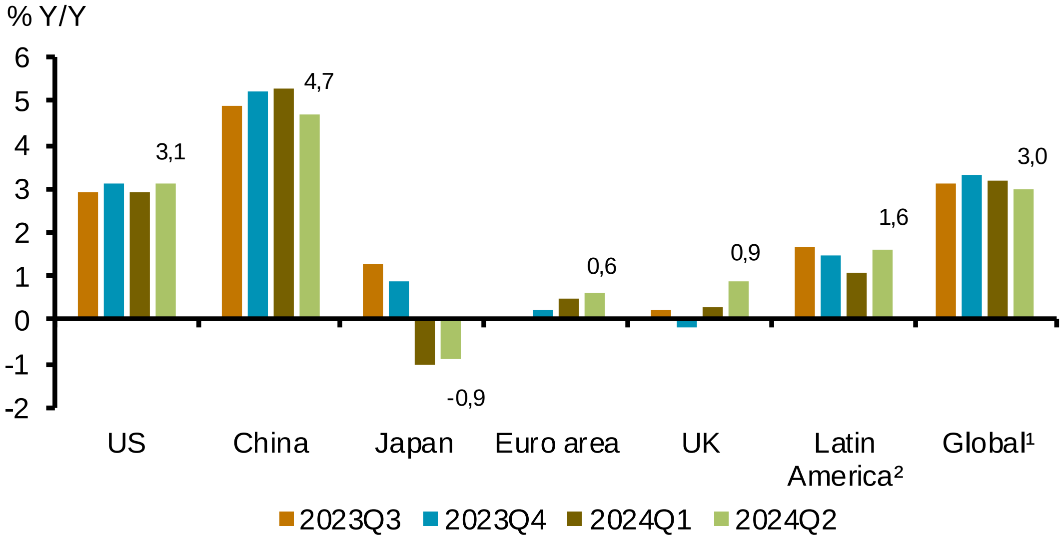
Economic outlook

External scenario

External outlook - Activity and inflation

The external environment is still characterized by the resilience of economic activity and the gradual continuation of the disinflation process.

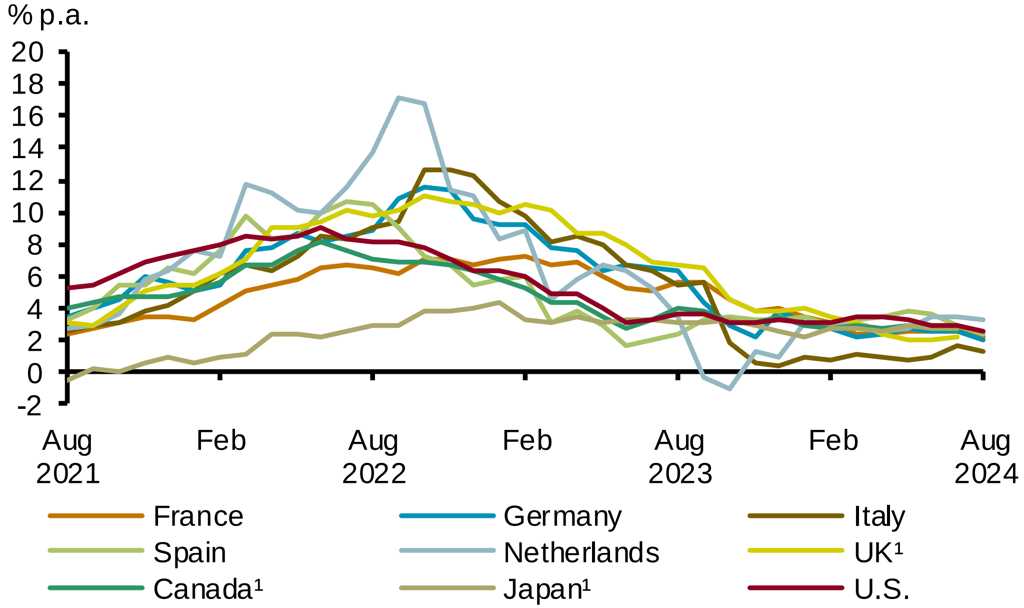
GDP growth
from 2023Q3 to 2024Q2



Sources: Bloomberg, BCB

1/ Calculated as described in the box "Projections and macroeconomic analysis model of the global economy" of the September 2022 IR.
2/ Argentina, Brazil, Chile, Colombia, Mexico, and Peru.

CPI – Advanced economies



Source: Bloomberg

1/ Until July 2024.

External scenario – Inflation

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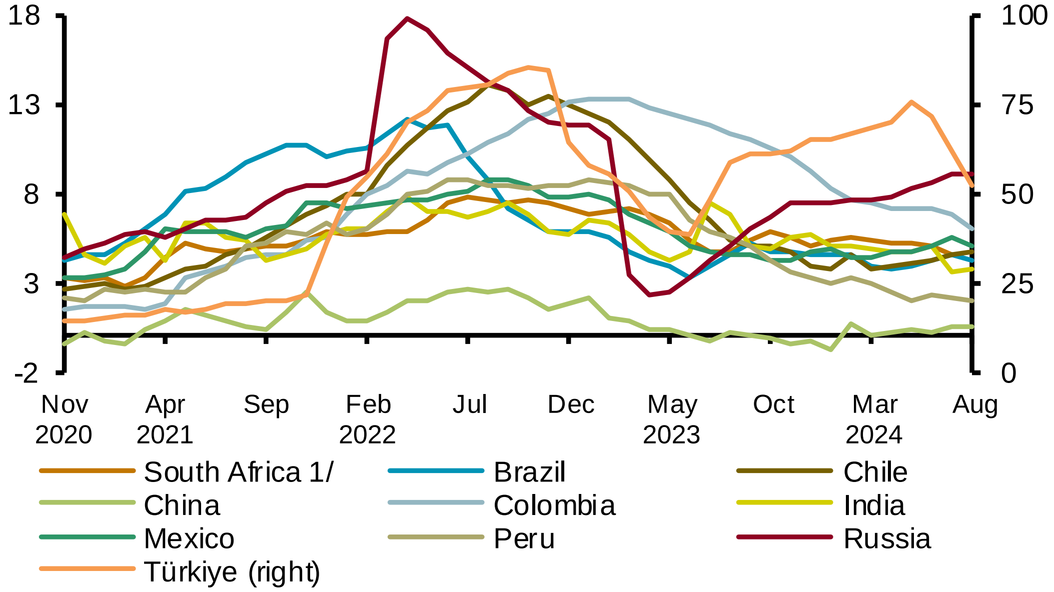
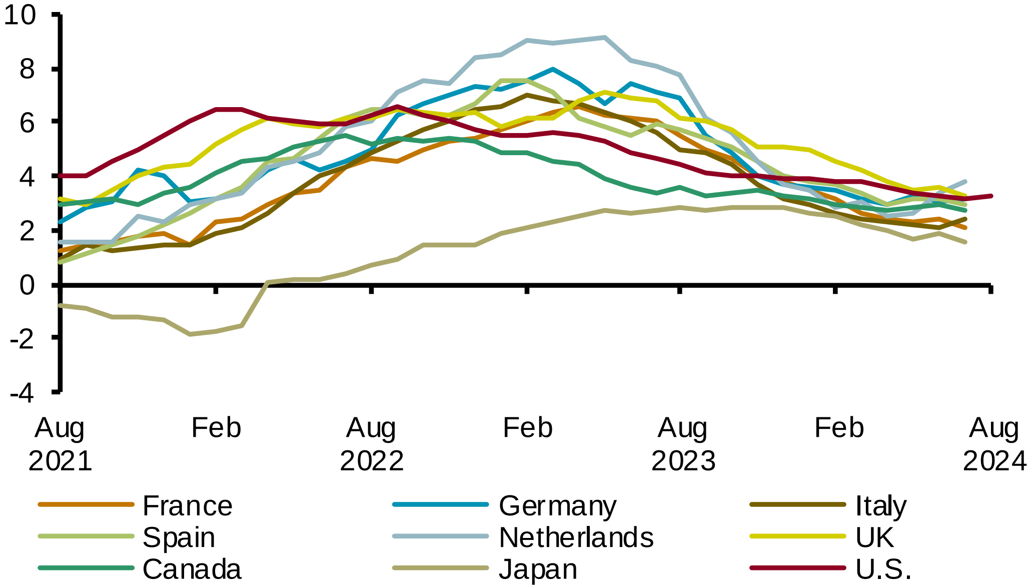
In emerging market economies, inflation rates continued to show distinct levels and trajectories, but with renewed pressures, particularly in food and beverages, and, to a lesser extent, energy. Core inflation is still at high levels and above the target in advanced economies.

CPI – Emerging markets



Source: Bloomberg
1/ Until July 2024.

CPI core – Advanced economies[1]

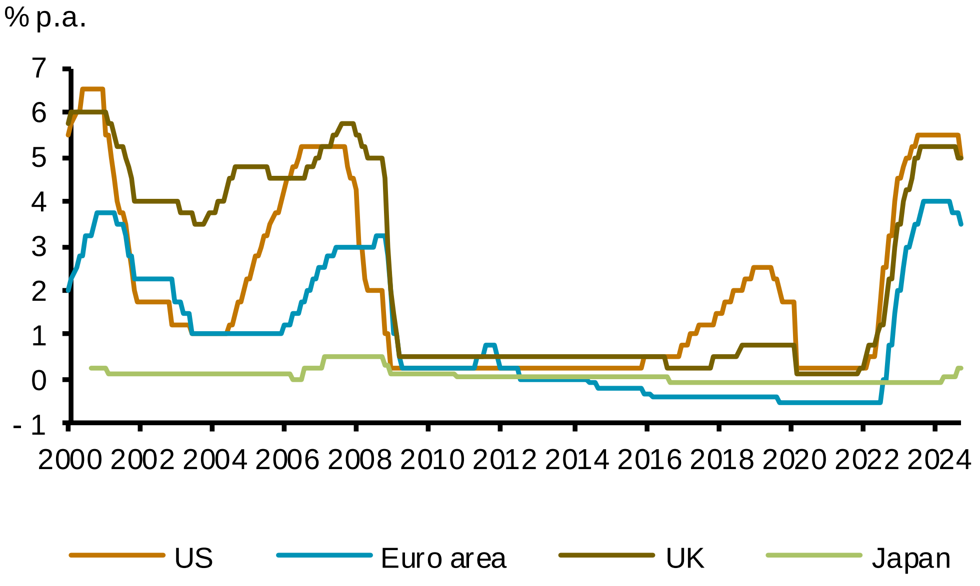


Source: Bloomberg
1/ U.S., until August 2024. Other countries until July 2024.

External scenario – Monetary policy and employment in the U.S.

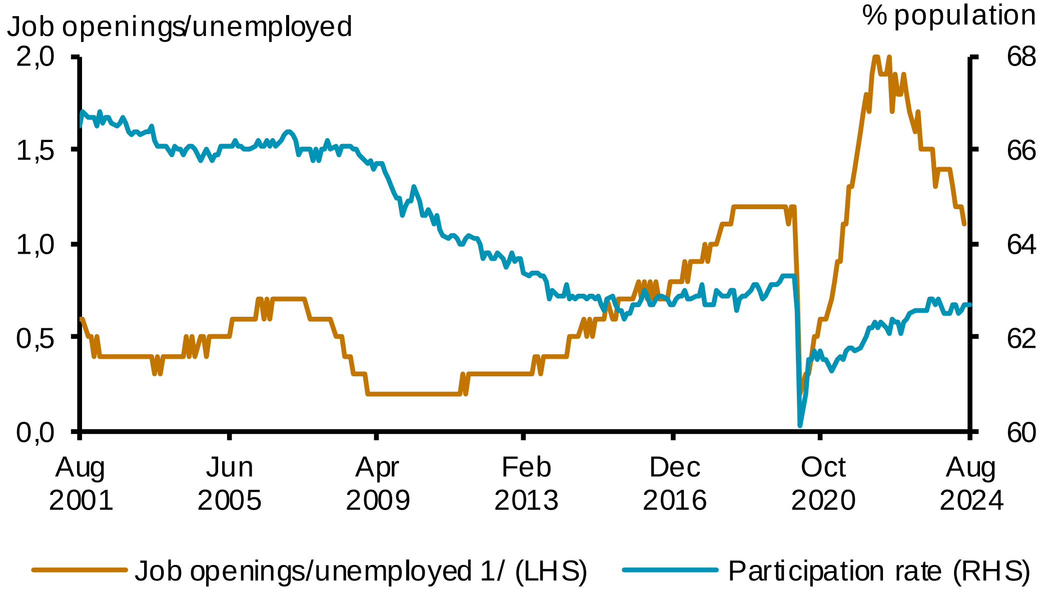
Global activity continues to show resilience notwithstanding the restrictive monetary policy, despite slowdown prospects. The labor market has become more balanced in recent months.

Monetary policy rates[1]



Source: Bloomberg
1/ Until September 18th.

U.S. – Job openings and participation rate

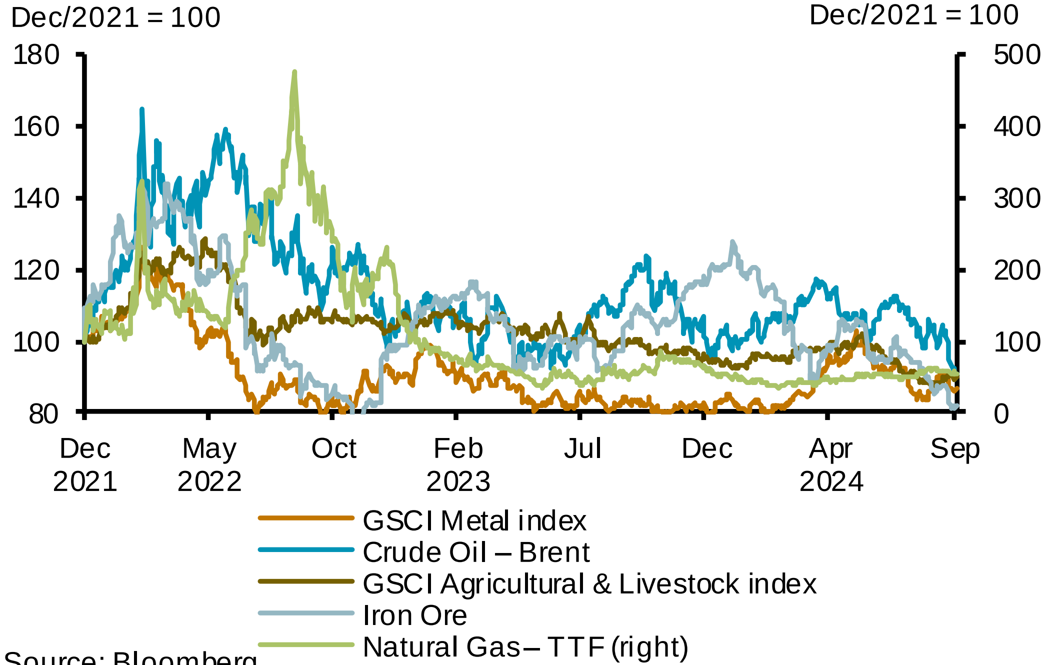


Source: Bloomberg
1/ Until July 2024.

External scenario – Commodities and pressure indicators

Energy commodity prices registered mixed dynamics, especially after the relief in oil prices. The prices of metal and agricultural commodities have also declined.

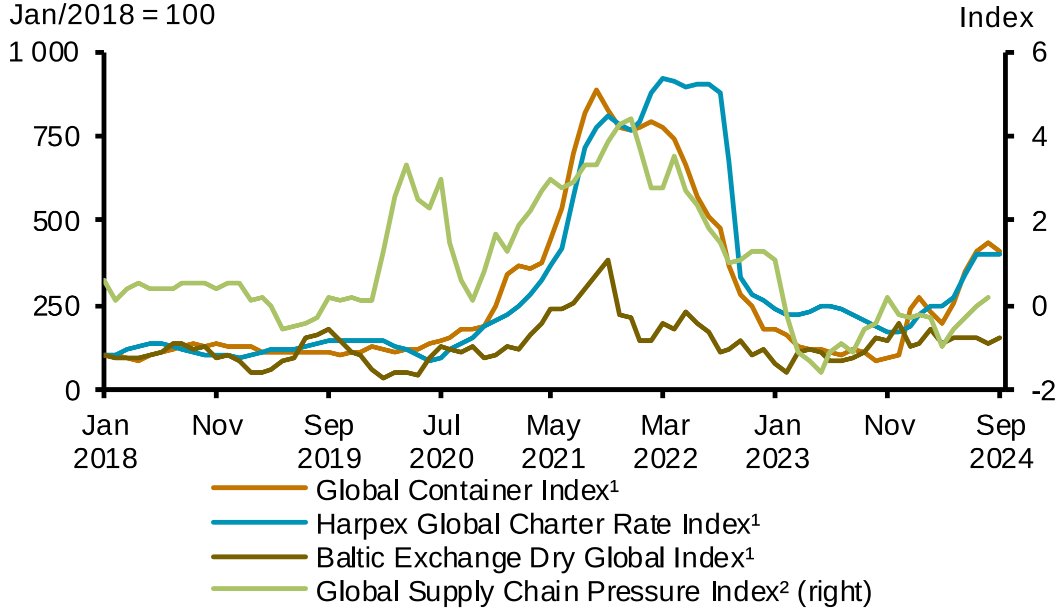
Commodity prices[1]



Source: Bloomberg

1/ Until September 11th.

Supply bottlenecks indicators



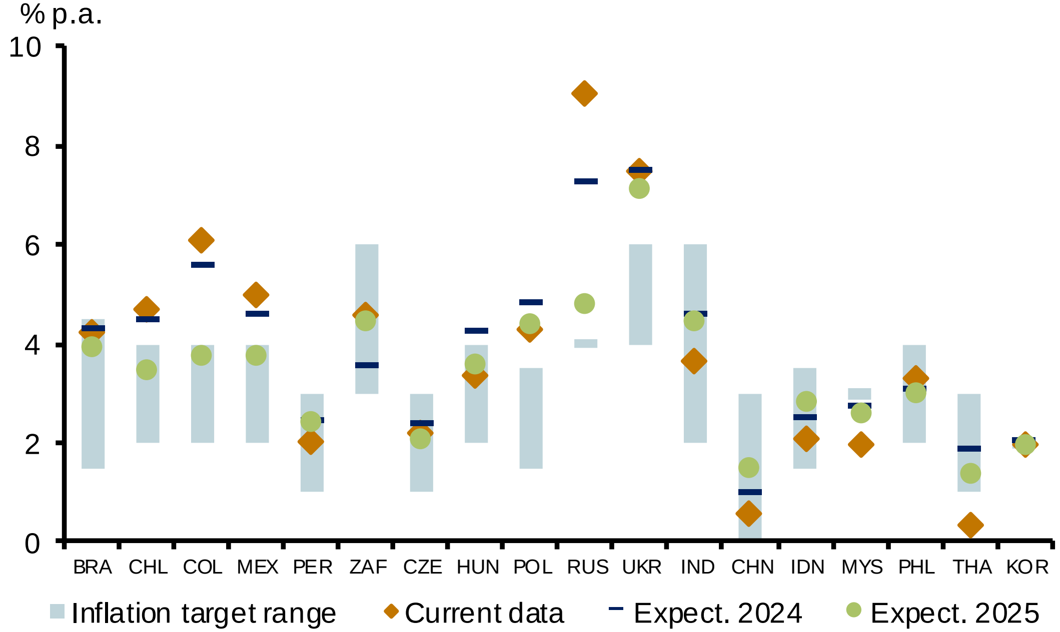
Sources: Refinitiv, Federal Reserve (Fed)

1/ Monthly averages - Until September 11th. 2/ Until August 2024.

External scenario – Expectations in emerging market economies

Expectations indicate inflation above the target at the end of 2024 in several emerging market economies.

Inflation expectations[1]



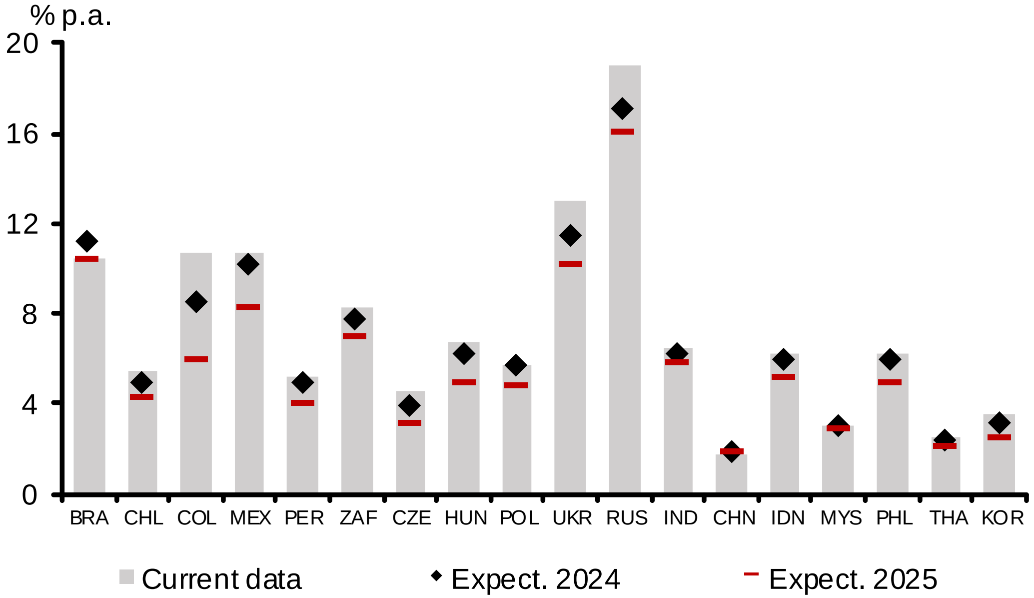
Sources: Bloomberg and central banks' surveys

1/ Until September 11th.

External scenario – Monetary policy in emerging market economies

Monetary easing is expected in emerging market economies, mainly in 2025.

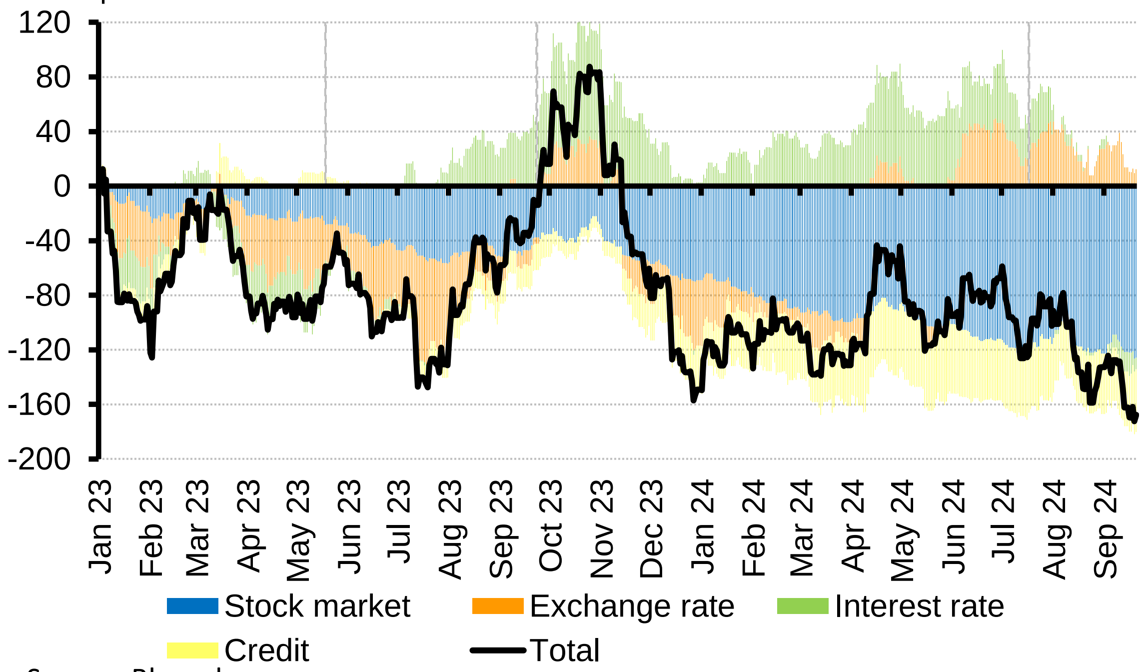
Policy interest rates[1]



Sources: Bloomberg and central banks' surveys
1/ Until September 11th.

Fed Funds equivalent of financial conditions

b.p. since Dec/2022



Source: Bloomberg

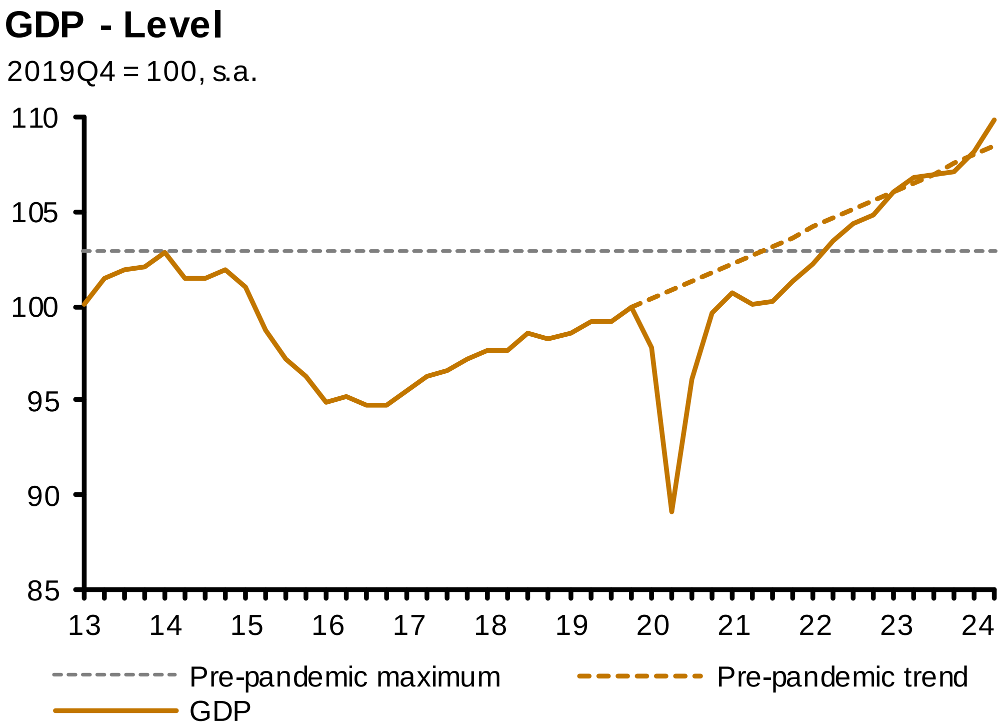
INFLATION REPORT (IR)

Economic outlook

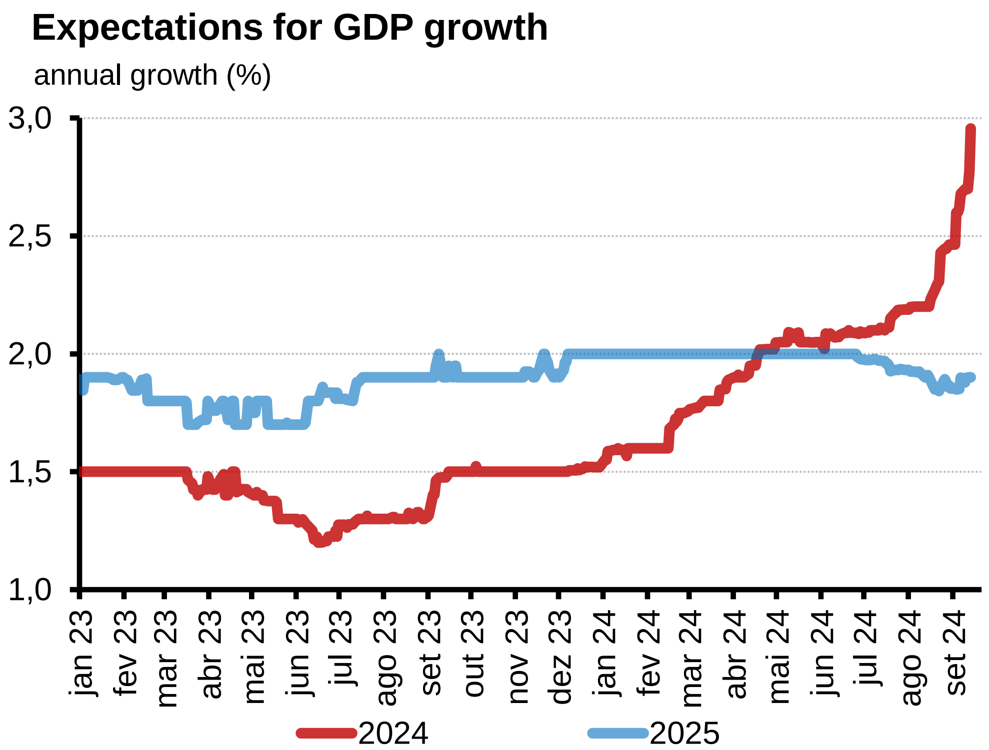
Domestic outlook

Economic activity

Brazilian economic activity remains dynamic, leading to a new round of upward revisions to growth projections for the year.



Source: IBGE

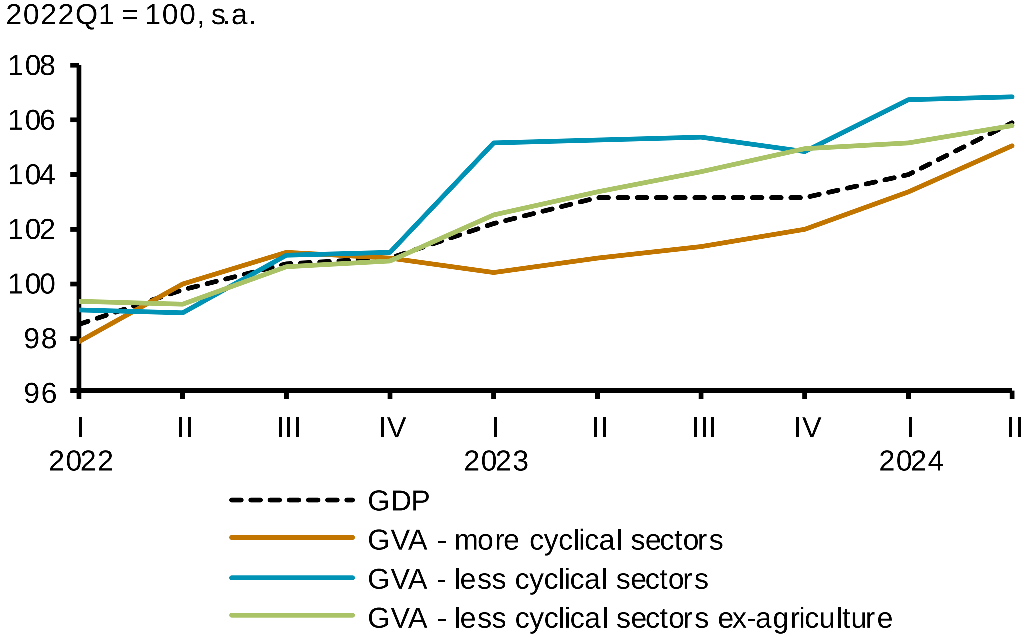


Economic activity

GDP growth in 2024Q2 by sectors was widespread and higher in the segments most sensitive to the economic cycle.

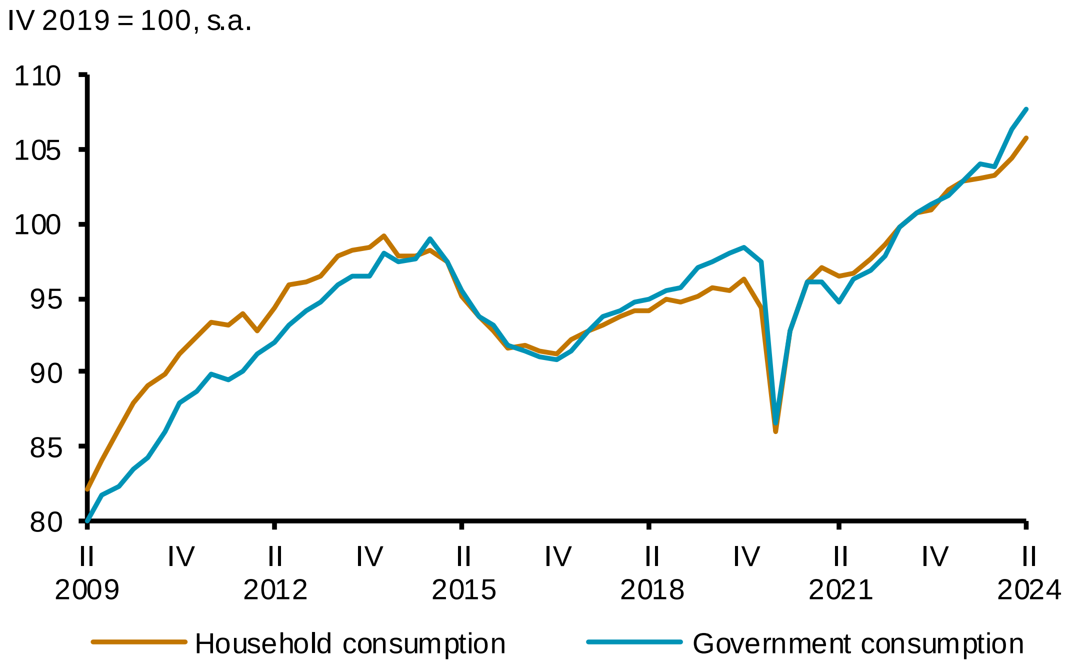
Growth in household consumption remains strong and, more recently, also reflects the recovery in durable goods. GFCF grew at high rates for the third consecutive quarter.

GDP – More and less cyclical sectors



Source: IBGE and BCB

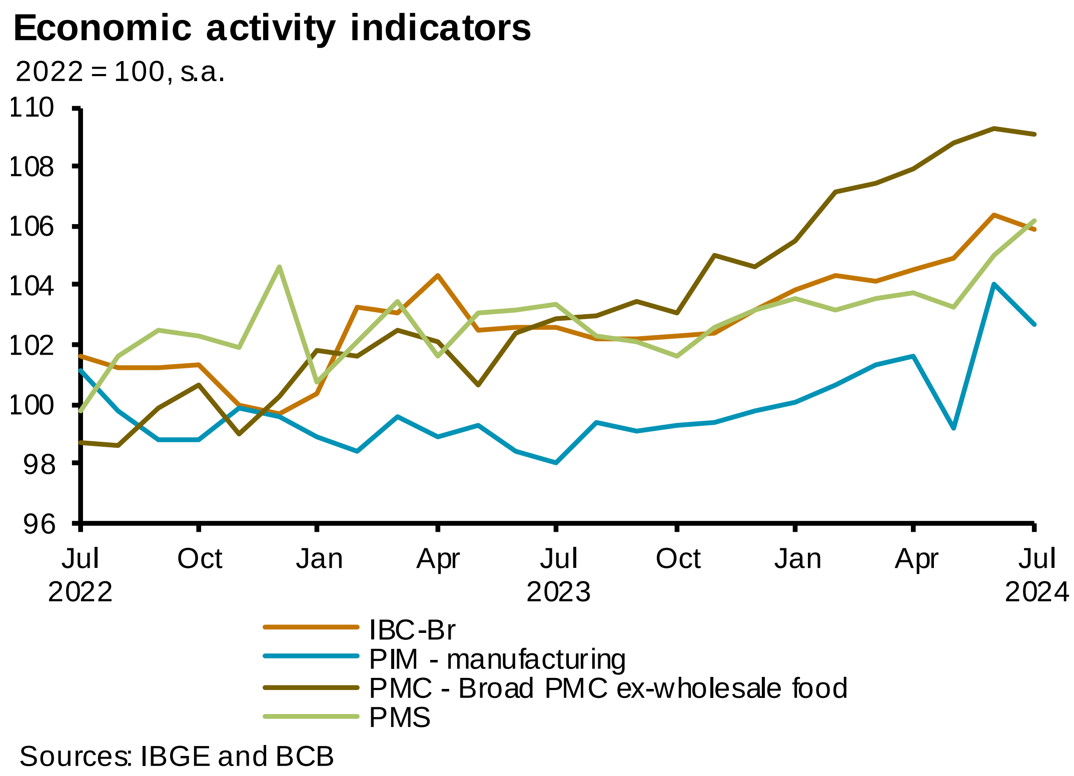
Gross Domestic Product – Demand



Source: IBGE

Economic activity

Monthly activity indicators generally suggest lower growth in 2024Q3.



BOX

GDP projection

Gross Domestic Product

Change %

	2023	2024[1/]		2025[1/]
		IR Jun	IR Sep	IR Sep
GDP at market prices	**2.9**	**2.3**	**3.2**	**2.0**
Taxes on products	2.1	3.4	4.7	1.9
Value added at basic prices	3.0	2.2	2.9	2.0
Supply				
Agriculture and livestock	15.1	-2.0	-1.6	2.0
Industry	1.6	2.7	3.5	2.4
Services	2.4	2.4	3.2	1.9
Demand				
Household consumption	3.1	3.5	4.5	2.2
Government consumption	1.7	1.8	2.7	2.0
Gross fixed capital formation	-3.0	4.5	5.5	2.0
Exports	9.1	0.5	3.2	2.5
Imports	-1.2	6.0	11.3	2.5
Net trade contribution (p.p.)	2.0	-0.9	-1.2	0.0

Source: IBGE and BCB

1/ Estimates.

2024

- **The GDP growth projection for 2024 rose from 2.3% to 3.2%.**
- **Growth above expectations in 2024Q2** led to a new round of upward revision to GDP growth projection for 2024.
- **A slower pace of growth is expected for the second half of 2024 and throughout 2025**, despite successive surprises.

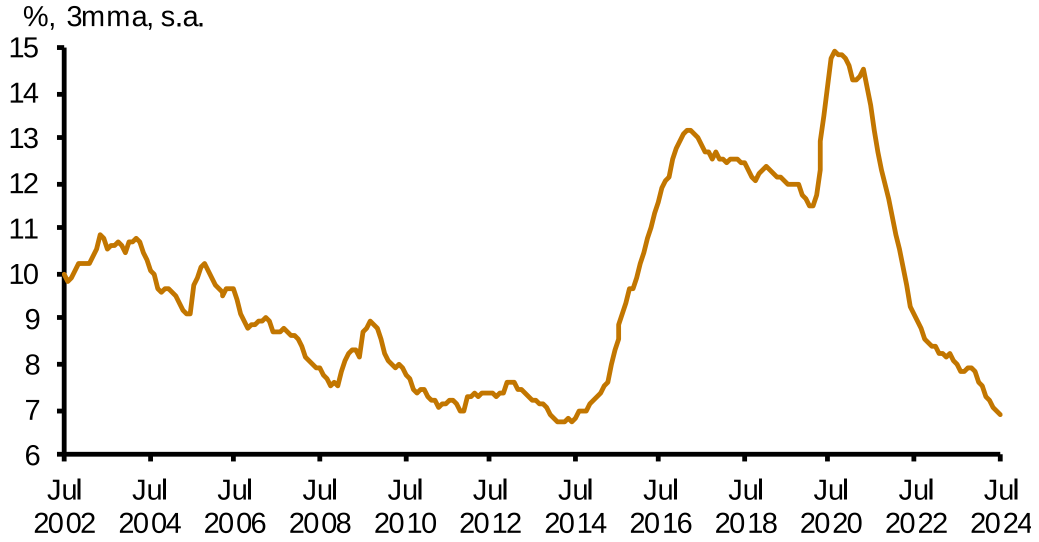
2025

- **The GDP growth projection for 2025 is 2.0%.**
- **Fairly homogeneous** changes are expected in supply and demand components, **generally lower than those expected for 2024**.

Labor market – Employment

The labor market has remained strong in recent months. The unemployment rate supported the downturn pace, and the creation of jobs has remained robust.

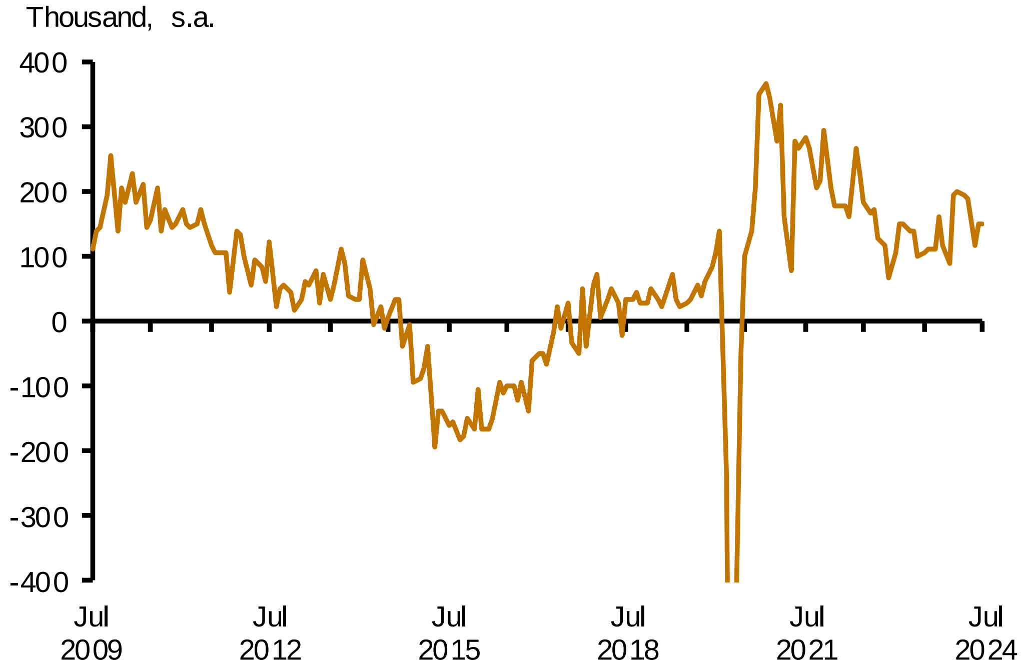
Unemployment rate[1]



[1] Historical unemployment rate estimates following Alves, S. A. L. and Fasolo, A. M., "Not Just Another Mixed Frequency Paper", Banco Central do Brasil (2015), Working Paper 400.

Sources: IBGE and BCB

Net formal job creation



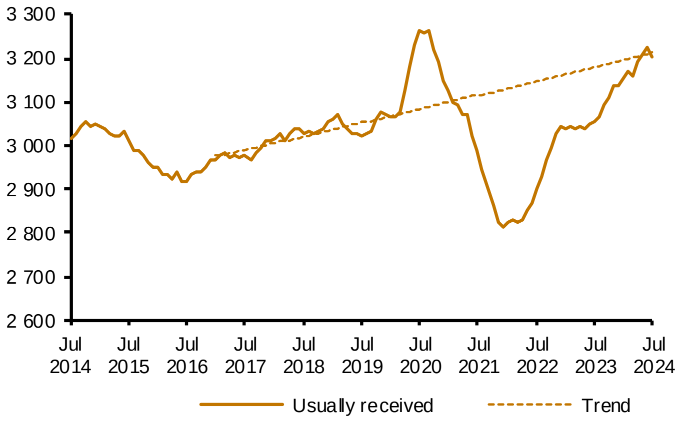
Source: Ministry of Labor and Employment

Labor market – Income

Average labor income measured by the PNAD Continuous continued to rise consistently, although slowing down. Other salary indicators, which have shown lower real growth than the PNAD throughout 2023, have not slowed down.

Real average labor income

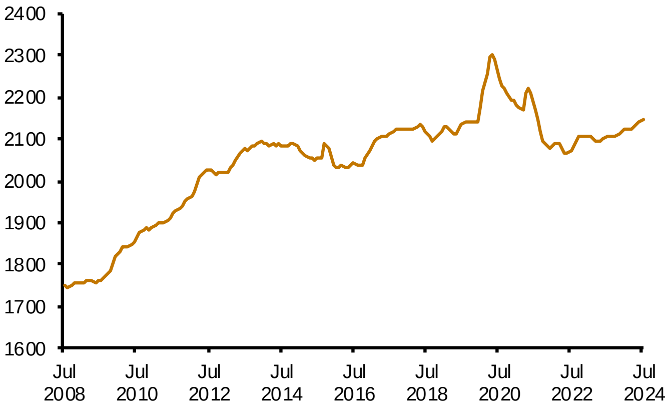
Mai-Jul 2024 BRL, 3mma, s.a.



Source: IBGE

Hiring salary

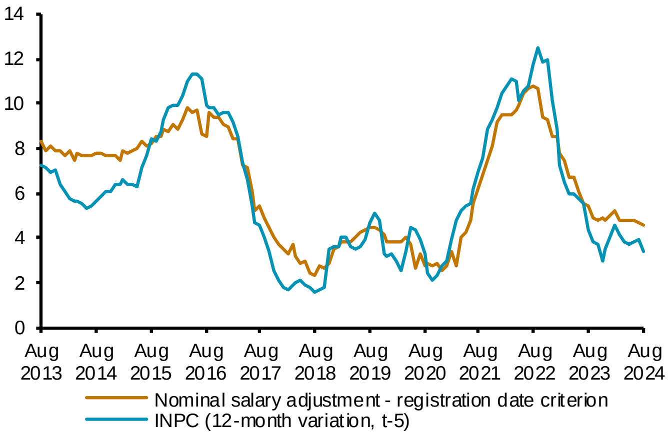
Jun 2024 BRL, 3mma, s.a.



Source: Ministry of Labor and Employment

Collective bargaining agreements

%



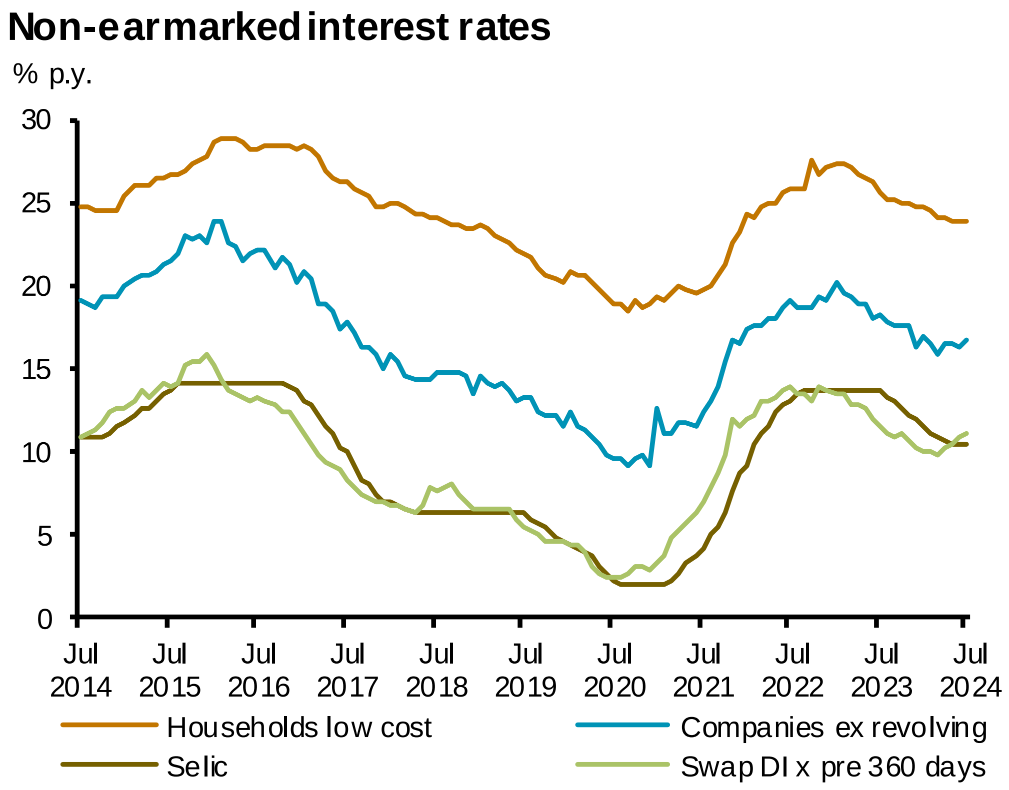
Sources: IBGE, MLE and BCB

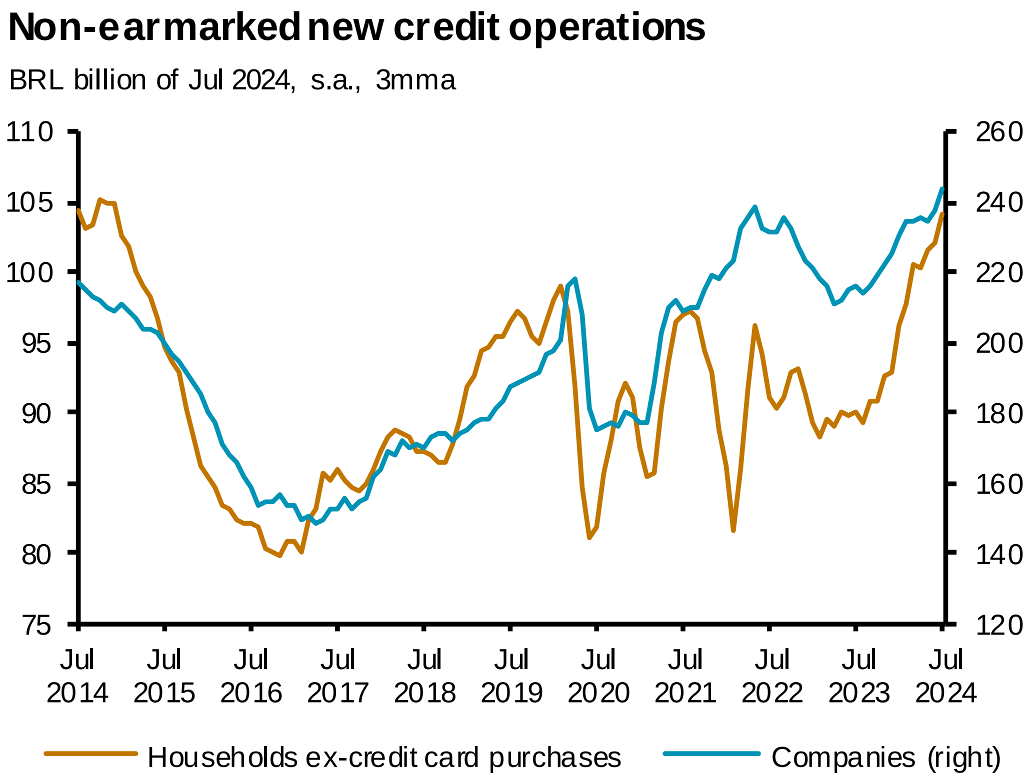
Complementary labor market indicators

- **The box presents several indicators that together corroborate the assessment that the labor market is heated.**
- Surprise drop in the unemployment rate.
- More comprehensive measures of labor force underutilization support a slack decrease.
- Employment growth driven by formal job creation.
- The increase of average income was fairly widespread across economic activities and types of occupation.
- Collective labor negotiations resulted in adjustments above inflation.
- Easier to find better job opportunities.
- Increased turnover rate and resignations.
- The shortage of skilled labor was the most cited limiting factor for the expansion of production in construction and services.

Credit

The credit market continued to show dynamism, with an expansion in non-earmarked credit granting and stable delinquency rates and improving supply and demand conditions.





Projection for credit growth in 2024 and 2025

- Nominal growth projection for the SFN credit balance in 2024 increased from 10.8% to 11.1%, driven by greater growth in non-earmarked credit portfolios, reflecting higher economic growth and a heated job market.
- For 2025, nominal growth is expected to decrease slightly to 10.3%.

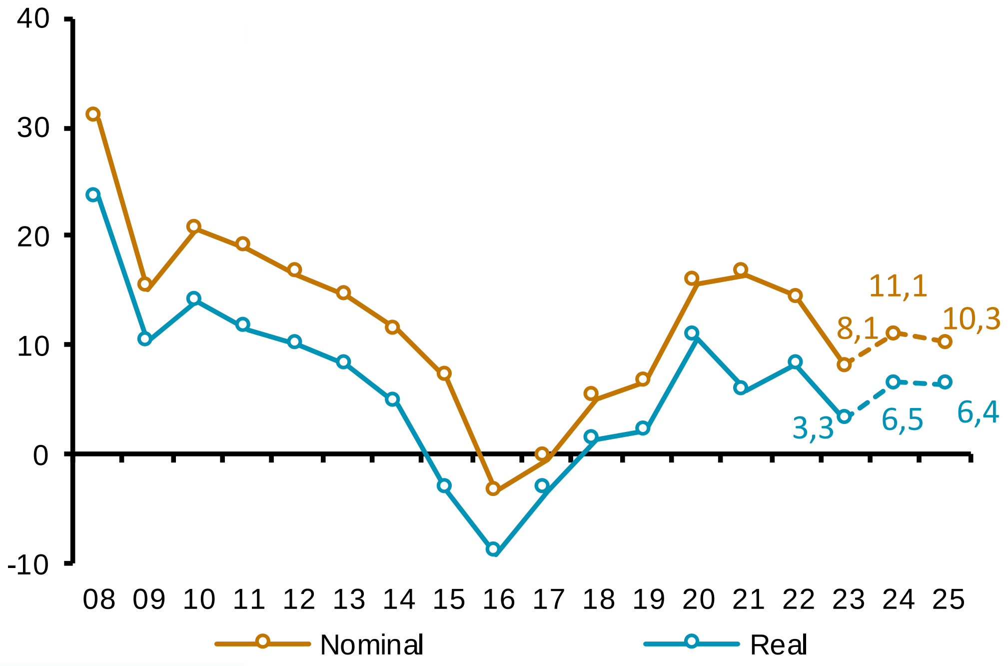
Credit balance

12-month % change

	Occurred			Proj. 2024		Proj. 2025
	2022	2023	Jul 2024	Previous	Current	Current
Total	14.5	8.1	10.3	10.8	11.1	10.3
Non-earmarke	14.9	5.5	8.6	10.0	10.5	10.2
Households	17.5	8.2	10.6	11.5	12.0	11.0
Corporations	11.9	2.1	6.1	8.0	8.5	9.0
Earmarked	14.0	11.9	12.7	12.0	12.0	10.5
Households	18.0	13.1	13.5	10.5	12.0	10.5
Corporations	6.9	9.6	11.1	15.0	12.0	10.5
Total Househ	17.7	10.4	11.9	11.0	12.0	10.8
Total Corpora	10.1	4.7	7.8	10.5	9.7	9.5

Total credit outstanding

% year change



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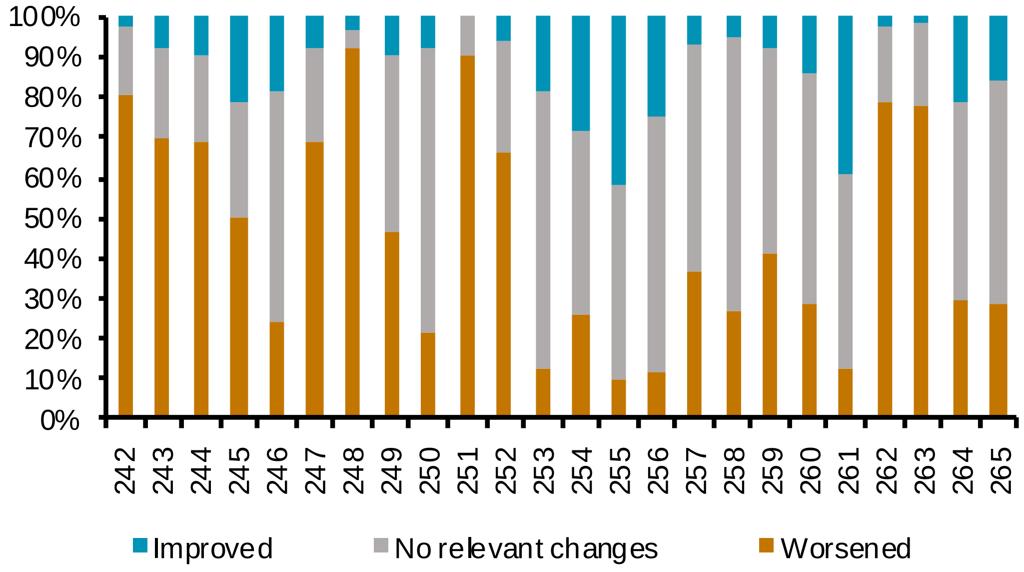
Fiscal

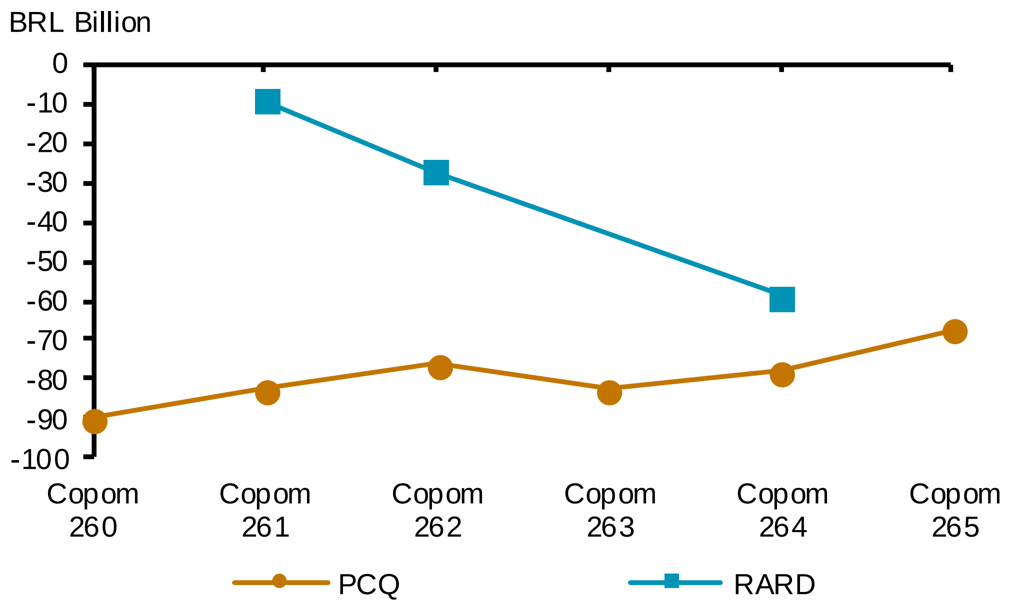
The government continues expecting to fulfill the primary balance target in the year, considering the tolerance interval. According to the PCQ, analysts' assessment is that the fiscal situation remained stable between the June and September Copom meetings, after worsening in 2024Q2.

PCQ: Assessment of fiscal situation



Question: How do you assess the change of the fiscal outlook since the previous Copom, considering both your baseline scenario and related risks?

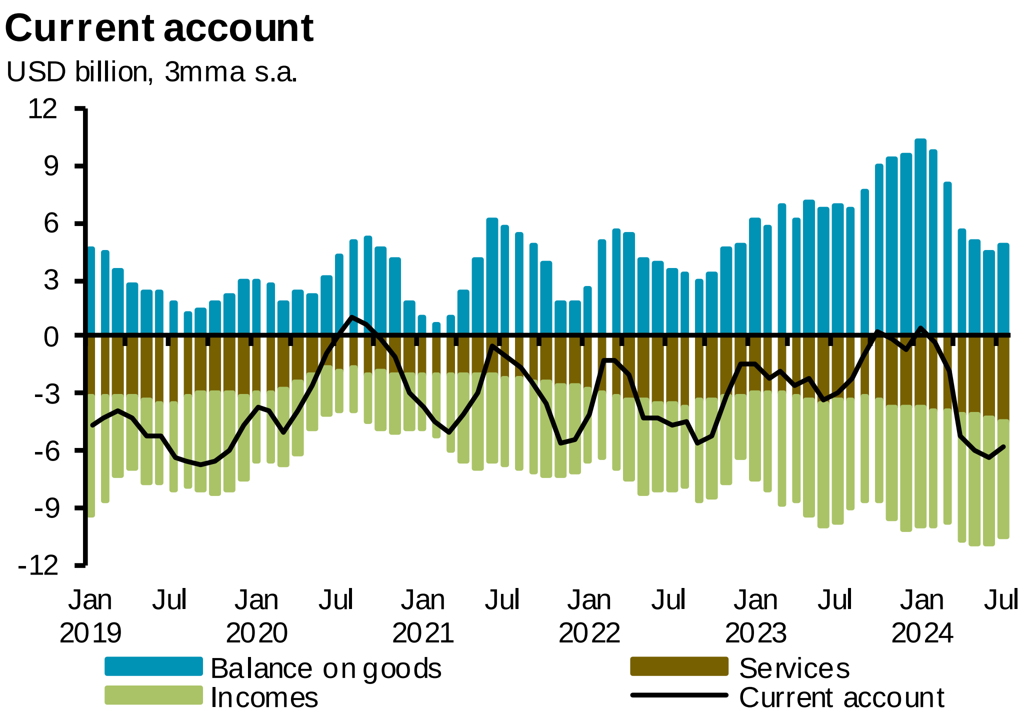
2024 Primary result forecast - Central Gov.

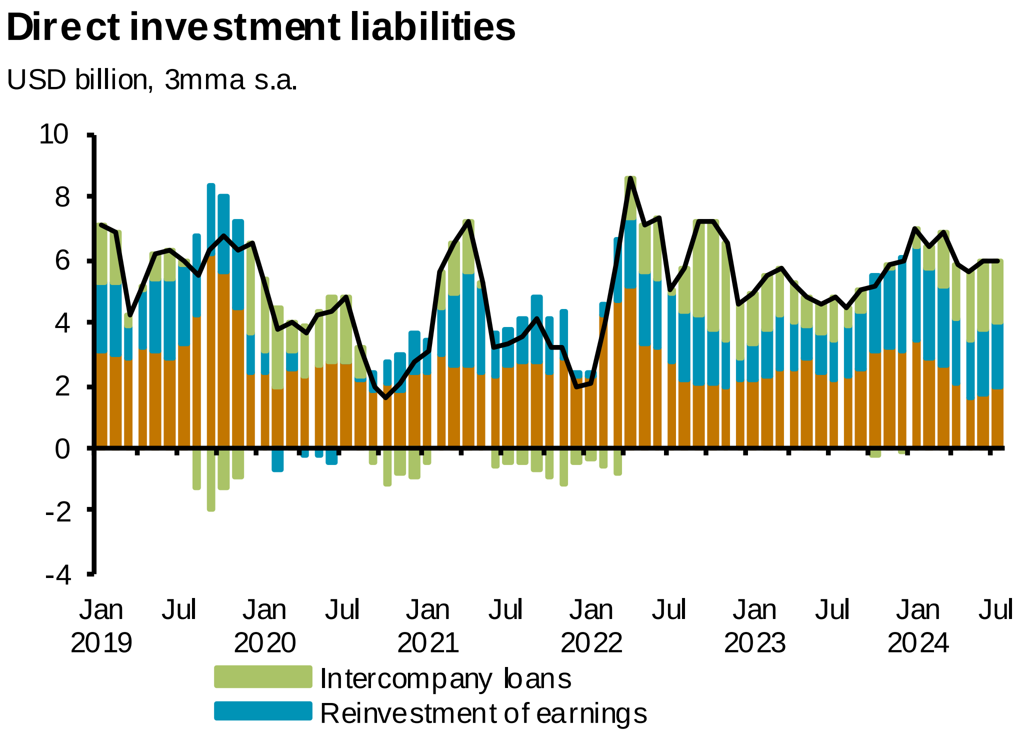


Sources: BCB and Ministry of Planning

External accounts

A still comfortable external accounts situation – characterized in recent months by increased current account deficit and stable net inflows of direct investment liabilities.





BOX

Projections for the 2024 and 2025 external accounts

USD billion

Itemization	2023	2024	2024 Forecast		2025 Forecast
	Year	Jan - Jul	Previous	Current	Current
Current account	-22	-26	-53	-51	-60
Balance on goods	92	45	59	68	64
Exports	344	200	335	335	341
Imports	252	155	276	267	277
Services	-40	-29	-43	-48	-49
of which: Travel	-8	-4	-9	-8	-10
of which: transportation	-13	-10	-14	-16	-15
Primary income	-76	-43	-71	-72	-75
of which: Interests	-28	-18	-29	-29	-31
of which: Dividens	-49	-26	-42	-43	-44
Investment - liabilities	85	82	75	102	85
DI liabilities	64	45	65	70	70
Portfolio investments	12	6	0	12	15
Other investments[1]	9	31	10	20	0

1/ includes loans, commercial credits, deposits and other investments

Current account deficit at 2.3% of GDP in 2024.

- Improvement in the trade balance compared with the June IR results from statistical reclassification of crypto assets;
- Increased expenses on freight and technology services;
- Moderate increase in direct investment liabilities projection. Portfolio Investment reflects good results in debt securities.

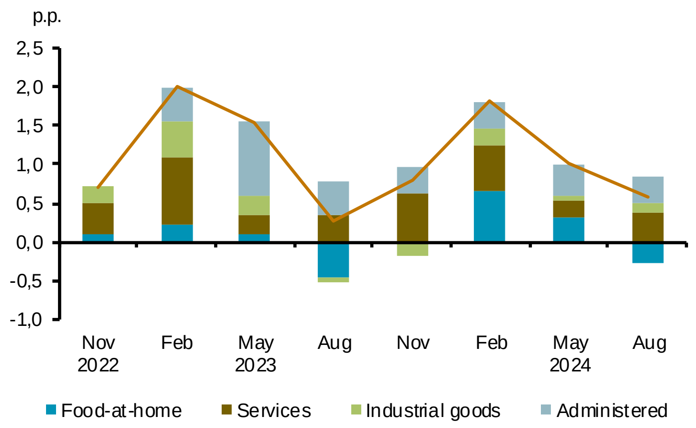
Current account deficit at 2.7% of GDP in 2025.

- Slight decrease in the trade balance with imports growing more than exports;
- Increase in primary income, with higher net expenses on interest and earnings and dividends.
- The expected current account deficit is still moderate and lower than projected net inflows of direct investment liabilities.

Consumer prices (IPCA)

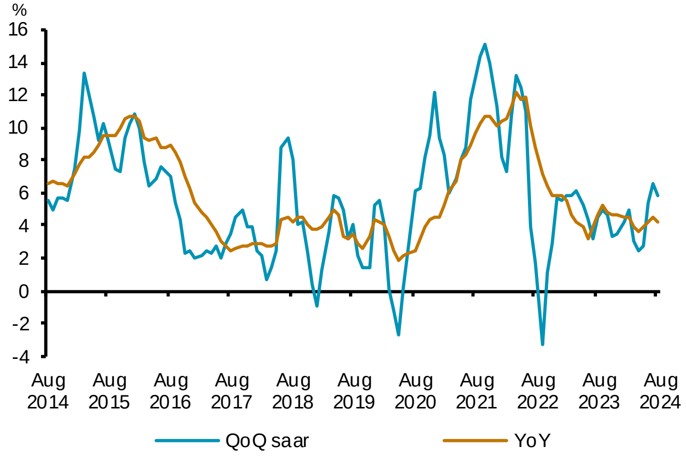
Consumer price inflation measured by the IPCA was lower in the Jun-Aug quarter, but core inflation and 12-month changes indicate a higher current inflation. The 12-month IPCA accelerated from 3.93% in May to 4.24% in August.

Contributions to IPCA quarterly changes



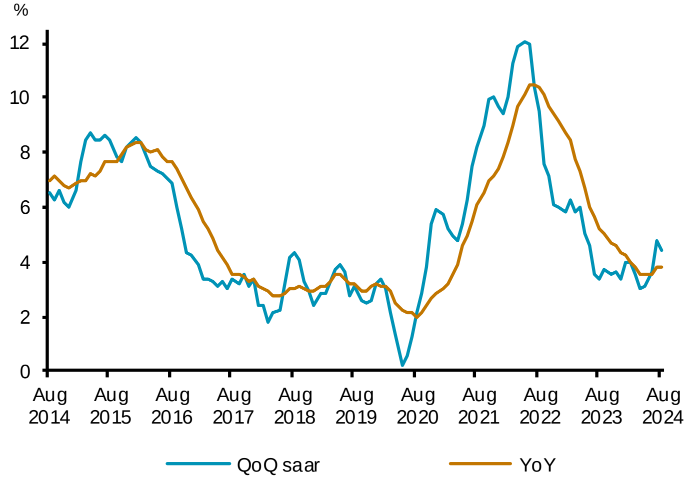
Sources: IBGE and BCB

IPCA



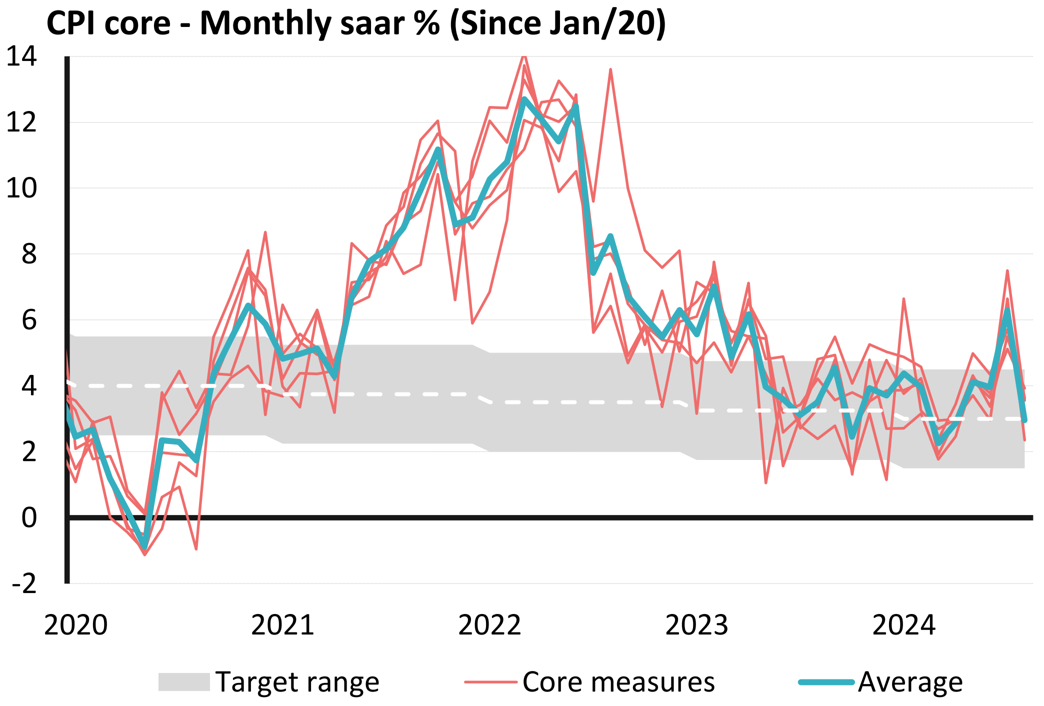
Sources: IBGE and BCB

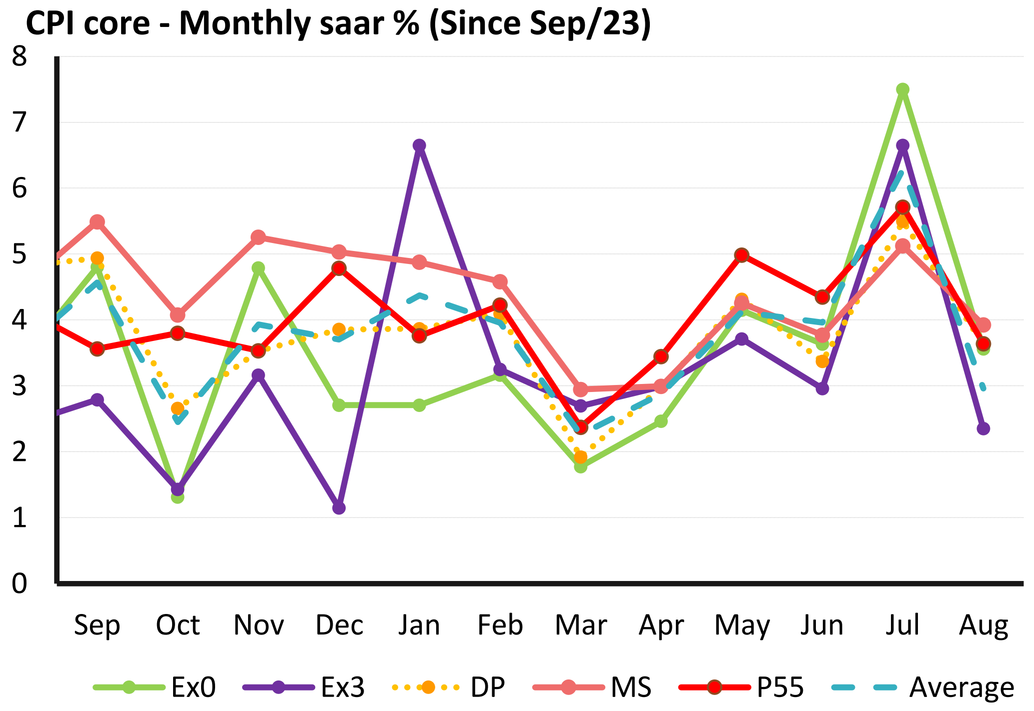
Average of core inflation measures



Consumer prices (IPCA)

Consumer inflation measured by the IPCA was lower in the Jun-Aug quarter but core inflation and 12-month changes indicate higher current inflation. The average 12-month core inflation rose from 3.55% in May to 3.80% in August.



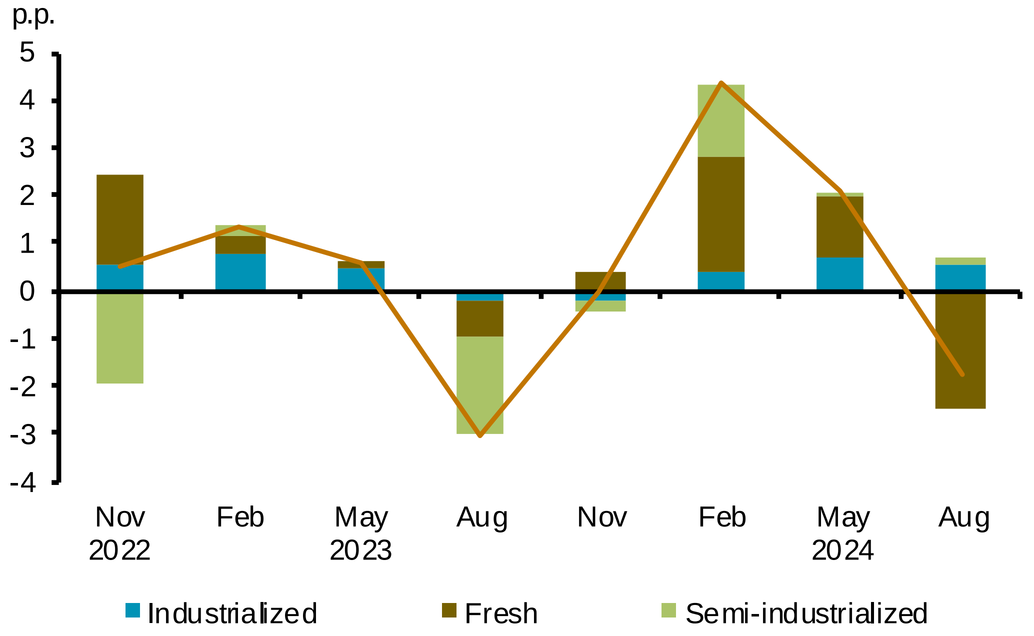


1/ The five measures discussed in the box "Update of the set of core inflation measures commonly considered by the BCB for economic outlook analysis" of the June 2020 Inflation Report are considered.

Consumer prices – Food-at-home

Food-at-home inflation dropped sharply in the Jun-Aug quarter, heavily influenced by the lower prices of fresh goods. Despite the favorable result in the quarter, the 12-month change in the segment continued to rise, reaching 4.60%, after declining in 2023.

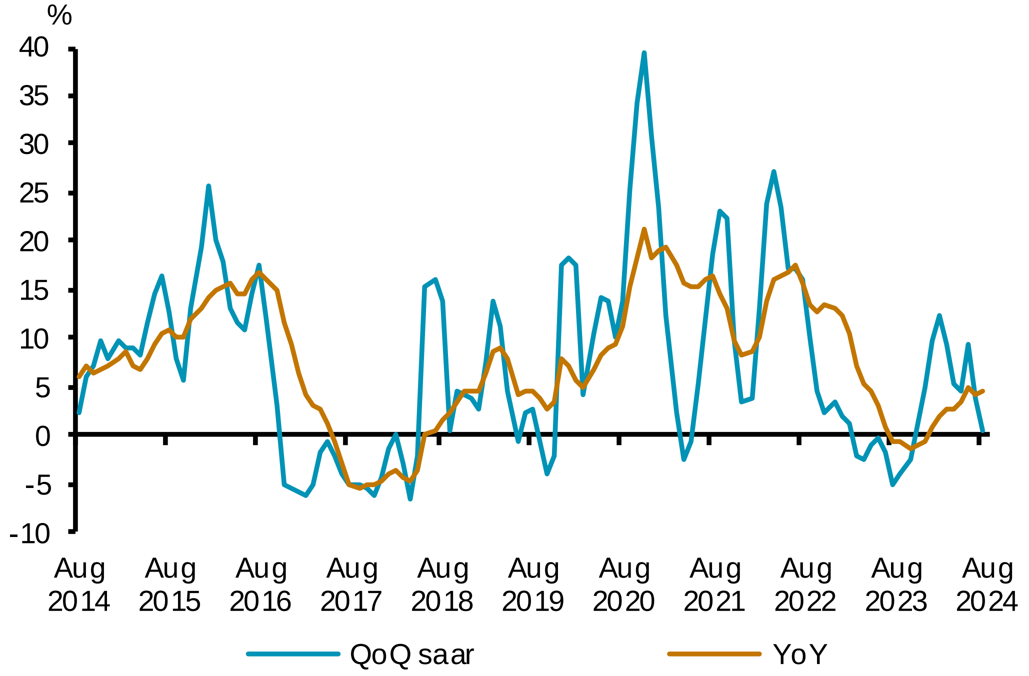
Contributions to quarterly changes in food-at-home prices – IPCA



Sources: IBGE and BCB

Food-at-home prices – IPCA

%

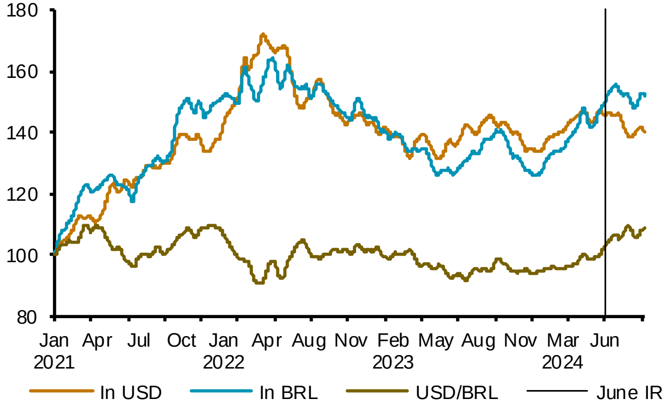


Consumer prices – Commodities and IPA

Commodity prices fell across the board, but increased when quoted in BRL due to the currency depreciation. Producer prices rose most strongly in manufacturing. The acceleration in producer prices may reflect the effects of the exchange rate depreciation seen in recent months.

IC-Br and foreign exchange rate

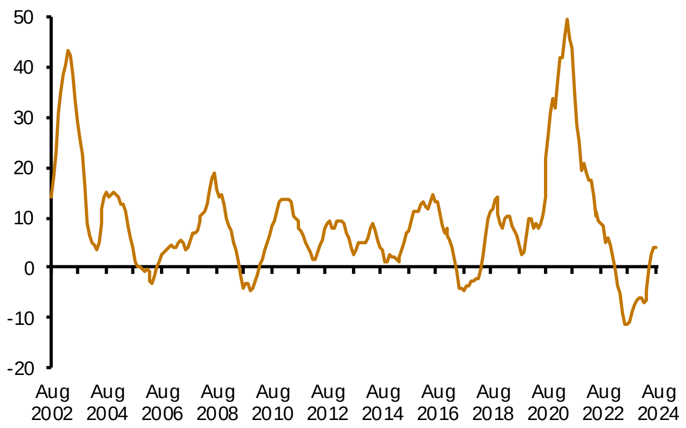
10-day moving average; Dec/31 2020 = 100



Sources: Bloomberg and BCB

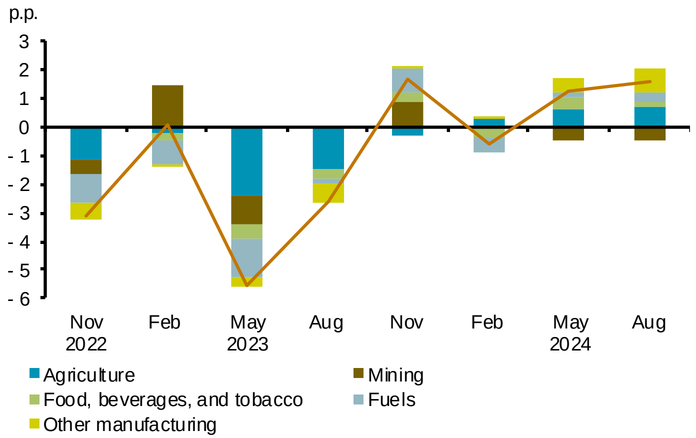
IPA-DI

%, YoY



Source: FGV

Contributions to quarterly IPA-DI change



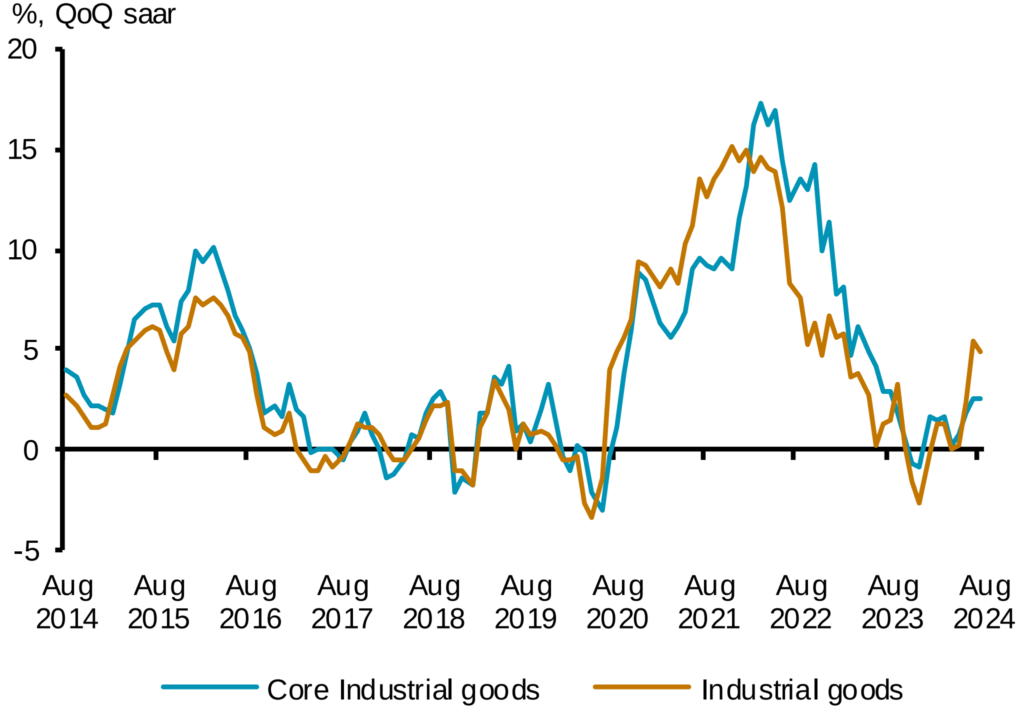
Source: FGV

Consumer prices – Industrial goods and services

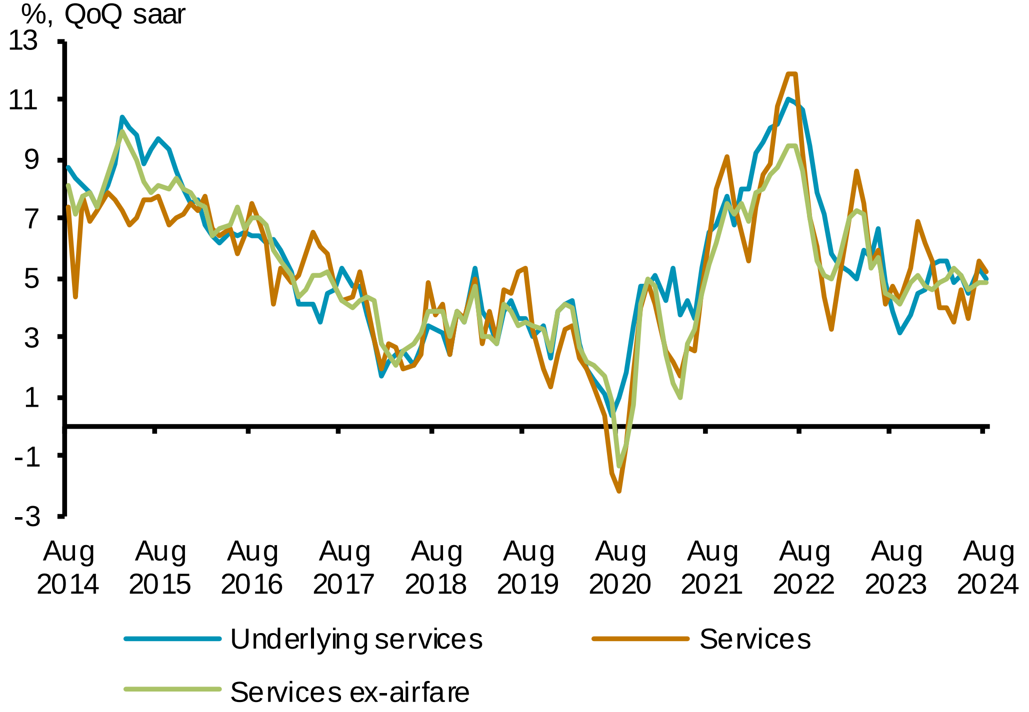
Changes of industrial goods prices were stronger, possibly associated with the pass-through of costs.

The increase of services prices was higher than in the previous quarter, and their underlying inflation measures remain at a high level.

Industrial goods inflation



Services inflation



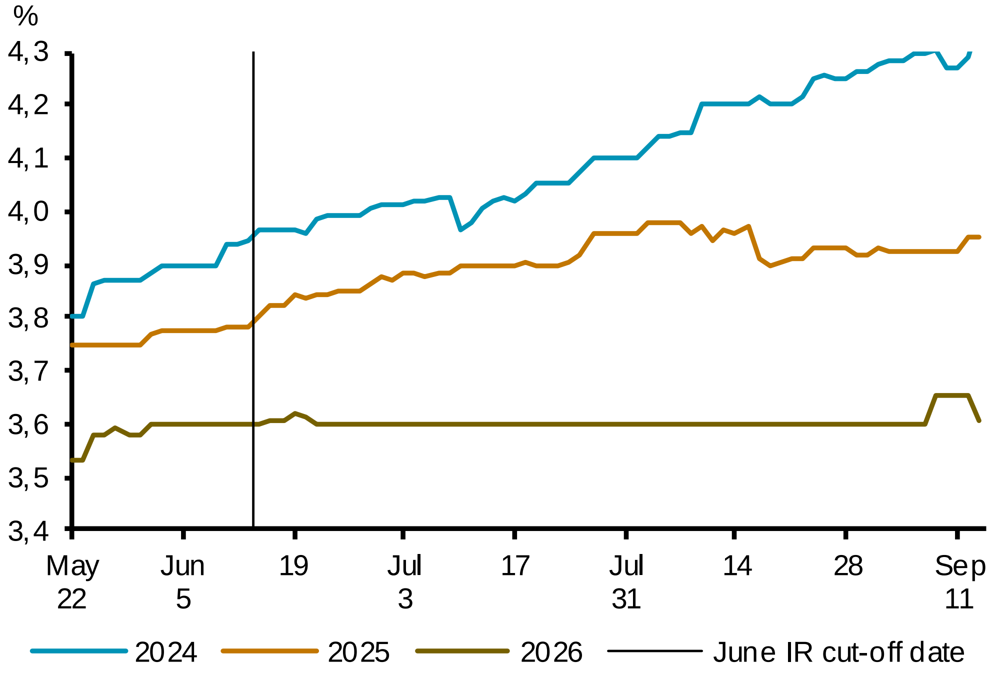
Consumer prices – Expectations

Inflation expectations for 2024 and 2025 have risen again, remaining unanchored for the following years.

Breakdown of the revision on the 2024 Focus survey

	Weights	Focus expectations (% p.a.)		
		Jun-14	Sep-13	Contr. to Δ (p.p.)
IPCA	**100**	**3.96**	**4.35**	**+0.39**
IPCA (by aggregation)	100	4.00	4.36	+0.35
Food-at-home	15	6.00	5.46	-0.08
Industrial goods	23	2.08	2.88	+0.19
Services	36	4.45	4.55	+0.04
Administered prices	26	3.95	4.78	+0.21
Market prices	74	4.00	4.19	+0.14
Market prices (by aggreg.)	74	4.02	4.21	+0.14

Median market expectations (Focus) – 2024, 2025, and 2026 IPCA



INFLATION REPORT (IR)

Inflation outlook

Short-term reference scenario

IPCA – Inflation surprise

% change

	2024				
	Jun	Jul	Aug	Quarterly up to Aug	12-month up to Aug
Copom scenario[1/]	0.33	0.12	0.07	0.52	4.19
Actual IPCA	0.21	0.38	-0.02	0.57	4.24
Surprise (p.p.)	-0.12	0.26	-0.09	0.05	0.05

Sources: IBGE and BCB

1/ Scenario at the June 2024 Inflation Report cut-off date.

IPCA – Short-term projections[1/]

% change

	2024			
	Sep	Oct	Nov	Dec
Monthly change	0.57	0.36	0.04	0.44
Quarterly change	0.93	0.91	0.97	0.84
12-month change	4.56	4.69	4.43	4.31

Sources: IBGE and BCB

1/ Copom's reference scenario at cut-off date.

Surprises

- Inflation in the Jun-Aug quarter was close to expectations, but with a different composition – lower in food and higher in other items, especially administered prices (fuels).
- The September projection was revised upwards, with higher change in food-at-home and transition to red energy tariff flag 1.

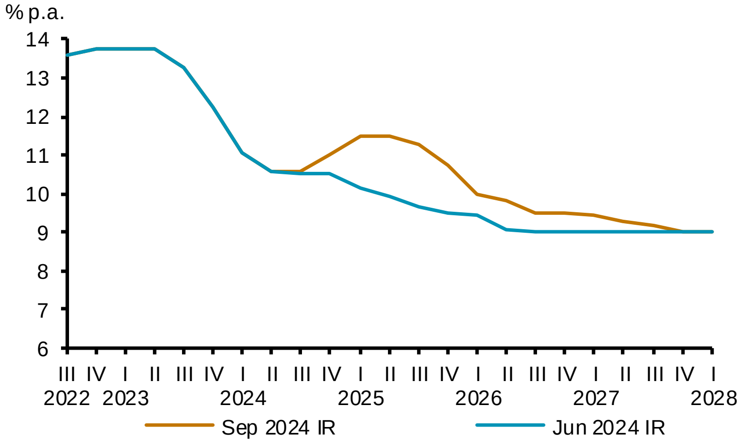
Projection

- The 12-month inflation is expected to remain close to the upper limit of the tolerance interval, amid higher monthly inflation rates.
- Factors contributing to the monthly inflation increase were food (unfavorable seasonality and drought), industrial goods (rising producer prices, exchange rate depreciation, and increase in cigarette taxes), and services (seasonal airfare increases). In administered prices: moderation in gasoline and increase in energy (tariff flags), but there is high uncertainty.

Conditional inflation projections: factors

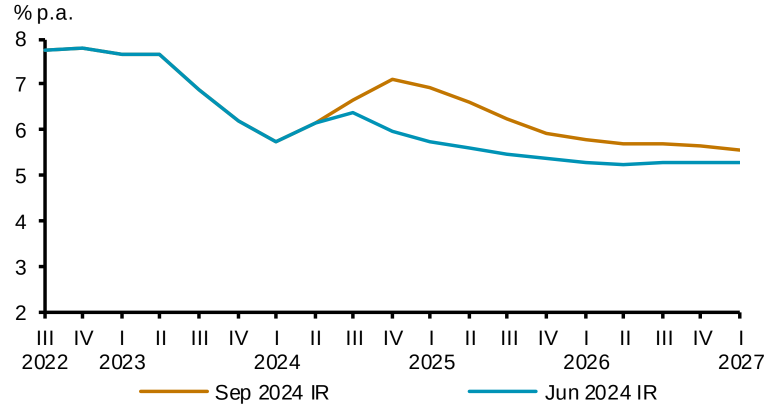
Selic rate target assumption for projections – Focus survey expectations

Quarterly averages



Four-quarter-ahead real Selic

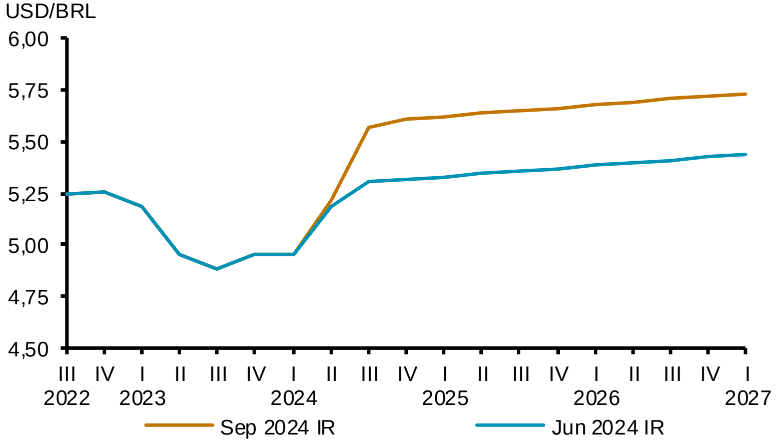
Quarterly averages



Note: Real Selic calculated as the four-quarter-ahead Selic rate, discounted from inflation expectations for the same period, both variables extracted from the Focus survey.

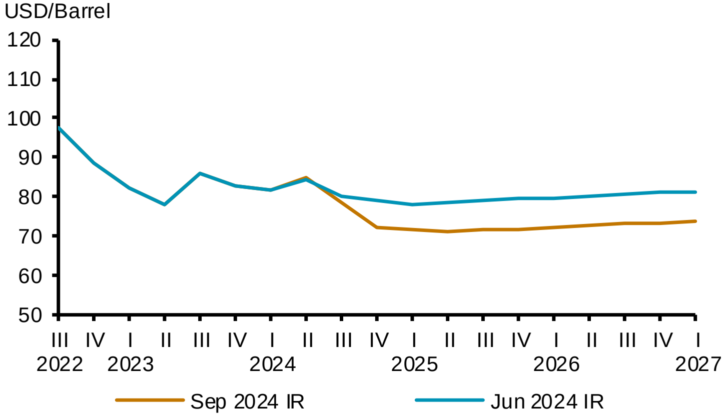
Exchange rate assumption for projections – PPP trajectory

Quarterly averages



Brent-type oil price

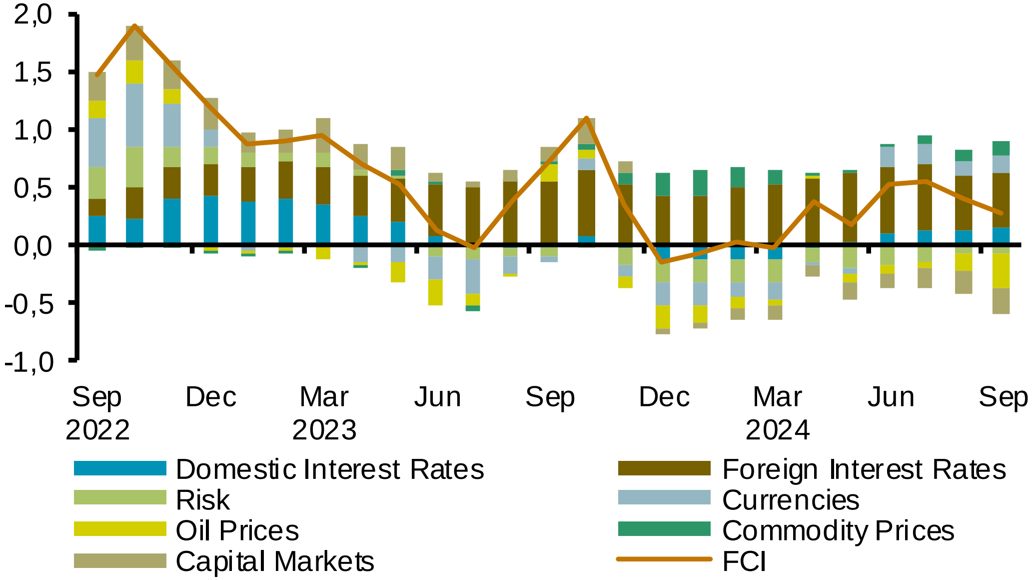
Quarterly averages



Sources: Bloomberg and BCB

Financial conditions

Financial Conditions Index
Standard deviations from the mean and contributions



Note: The higher the value of the index, the tighter the financial conditions. Values refer to monthly averages. Sep/2024 value refers to the average until the 13th.

Financial conditions has become more restrictive at the beginning of 2024Q3 and subsequently cooled.

Key factors for the FCI decline in the quarter:

- reduction in external future interest rates;
- oil price drop;
- domestic stock exchange valuation;
- USD depreciation against currencies of other advanced economies

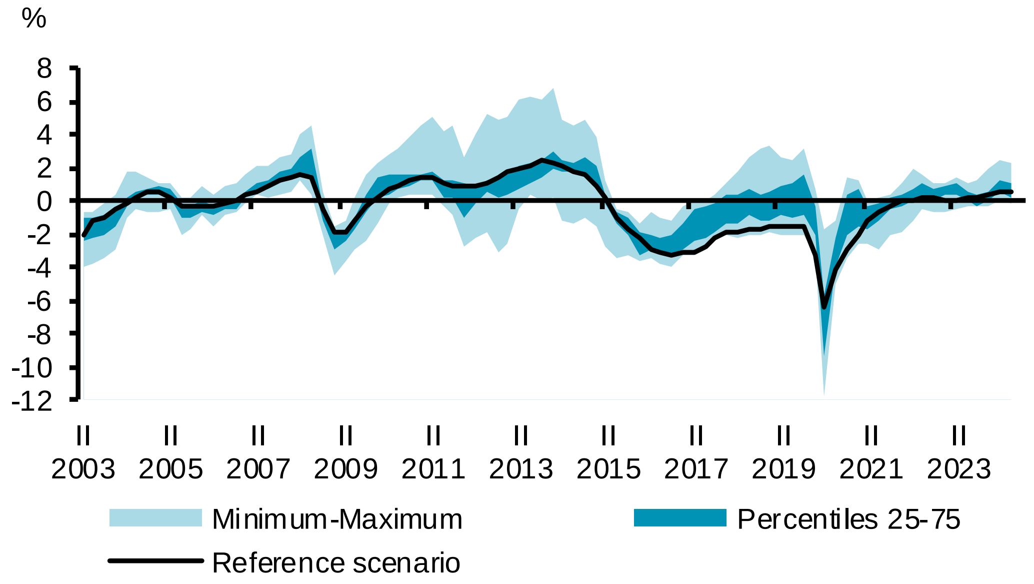
Key factors for the FCI increase in the quarter:

- rise in domestic short-term future interest rates;
- BRL depreciation;
- VIX increase;
- decline in agricultural and metal commodity prices.

Output gap

Significant surprises economic activity surprises=> output gap reassessed upwards
Output gap: from neutral to positive

Output Gap: estimates and dispersion



Note: Dispersion measures were constructed using a set of output gap measures. See the box "Output gap measures in Brazil", in the June 2024 Report, for a presentation of various methodologies. Chart data: 2003Q2–2024Q3.

- The estimated output gap for 2024Q3 and 2024Q4 are 0.5% and 0.3%, respectively.
- The estimated output gap for 2026Q1 is -0.3%.

Governance for the communication of the inflation projections horizon

Projection horizon presented in the quarterly reports of central banks

Central bank	Document	Horizon	Horizon length ahead (in quarters)
South Africa	Monetary Policy Review	Calendar year	9 and 11
Australia	Statement on Monetary Policy	Half year	8 and 9
Canada	Monetary Policy Report	Calendar year	8 to 11
Chile	Informe de Política Monetaria	Calendar year	8 to 11
Colombia	Informe de Política Monetaria	Fixed-length	8
South Korea	Monetary Policy Report	Calendar year	5 to 8
United States	Projection Materials	Calendar year	10 to 13
Japan	Outlook Report	Calendar year	8 to 11
Mexico	Informe Trimestral	Fixed-length	8
New Zealand	Monetary Policy Statement	Fixed-length	12
Peru	Reporte de Inflación	Calendar year	5 to 8
United Kingdom	Monetary Policy Report	Fixed-length	12
Czech Republic	Monetary Policy Report	Calendar year	6 to 9
Sweden	Monetary Policy Report	Calendar year	9 to 12
Euro area	Staff Macroeconomic Projections	Calendar year	9 to 12

- It is necessary to establish a new governance for communicating the inflation projection horizon in line with the new continuous inflation target system.
- Countries' experience:
  - fixed-length horizon;
  - variable-length horizon ending in a calendar year.
- The ten-quarter fixed-length is the governance adopted for the inflation projections horizon:
  - it covers the current relevant horizon;
  - it considers that the uncertainty increases as the horizons extends;
  - this horizon length is in line with most of the analyzed countries.

Conditional projections for inflation: reference scenario

BANCO CENTRAL DO BRASIL

Inflation projections – Reference scenario
YoY IPCA inflation

%

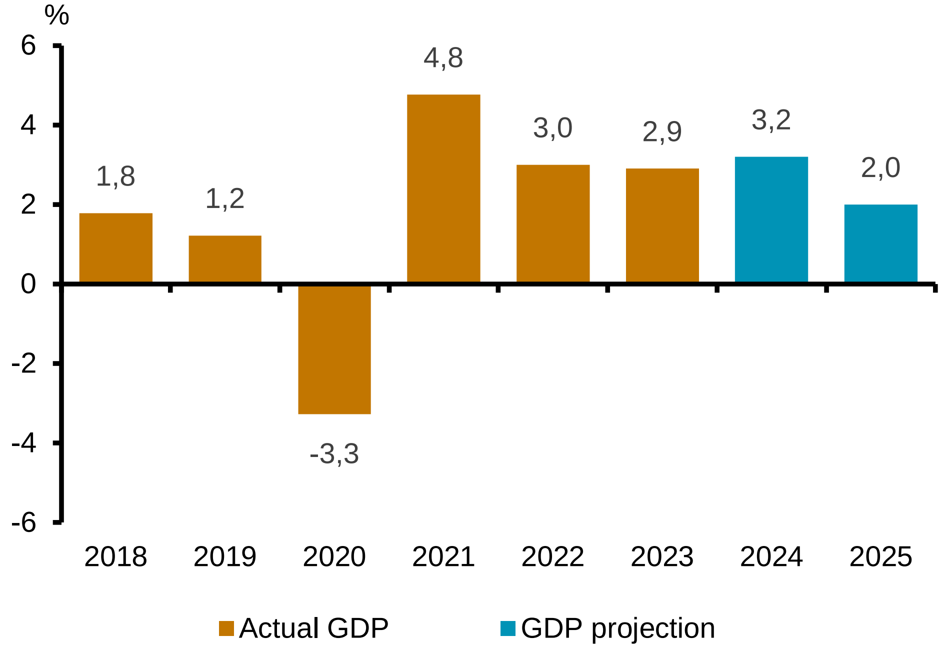
	2023		2024				2025				2026				2027
Price index	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I
IPCA	5.2	4.6	3.9	4.2	4.6	4.3	4.0	3.8	3.5	3.7	3.5	3.5	3.4	3.3	3.2
Previous IR difference (p.p.)	[0.0]	[0.0]	[0.0]	[-0.2]	[0.5]	[0.3]	[0.2]	[0.5]	[0.1]	[0.3]	[0.2]	[0.3]	[0.2]	[0.1]	-
Market prices	3.5	3.1	3.1	3.5	4.3	4.4	4.3	4.1	3.8	3.6	3.4	3.3	3.2	3.1	3.1
Previous IR difference (p.p.)	[0.0]	[0.0]	[0.0]	[-0.2]	[0.2]	[0.5]	[0.7]	[1.0]	[0.7]	[0.4]	[0.2]	[0.2]	[0.1]	[0.0]	-
Administered prices	10.2	9.1	6.4	6.4	5.3	4.2	3.3	2.8	2.5	4.0	3.9	4.1	3.8	3.8	3.6
Previous IR difference (p.p.)	[0.0]	[0.0]	[0.0]	[0.2]	[1.2]	[-0.2]	[-0.8]	[-1.3]	[-1.6]	[0.0]	[0.2]	[0.6]	[0.3]	[0.3]	-

Note: Shaded areas indicate projections. The values presented are rounded; therefore, the aggregated values may not match the combination of the rounded disaggregated values. The difference with respect to the previous Report is calculated using the rounded values.

- Inflation, after rising in 2024Q2 and 2024Q3, resumes a downward path, still remaining above the target.
- Inflation projections have risen in the entire horizon, increasing the distance from the target
- Key factors for rising projections:
    - Stronger-than-expected economic activity => increasing expected output gap
    - Currency depreciation
    - Inflation expectations increase
- Key factors for reducing projections:
    - Oil price drop
    - Real interest rate increase

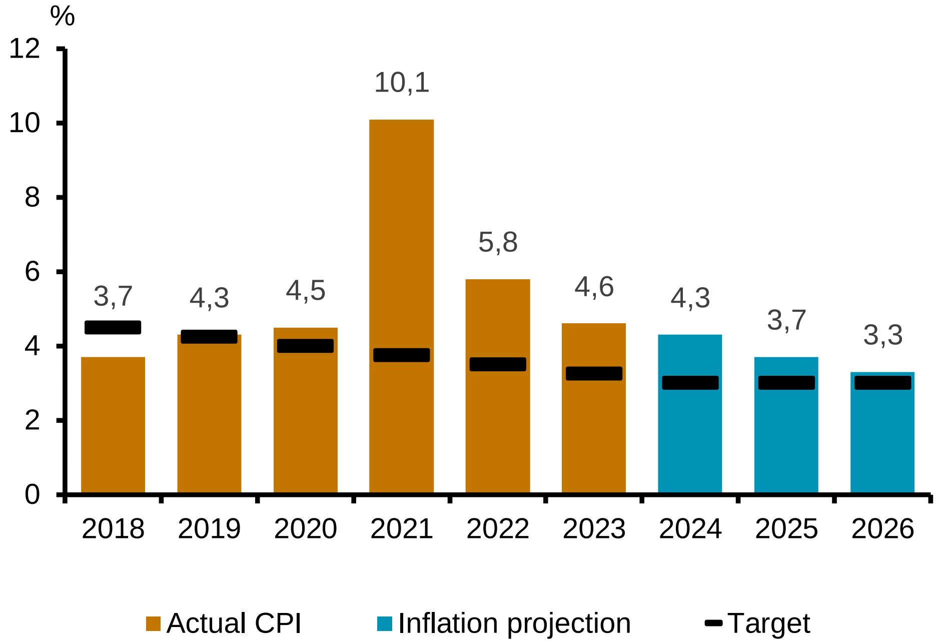
GDP and IPCA projections

Actual GDP and GDP projection



Sources: IBGE and BCB

Actual CPI and inflation projection – IPCA



Sources: IBGE and BCB

Final remarks – balance of risks

- The Committee judges that the risks to its inflation scenarios are tilted to the upside.

- Among the risks to the inflation scenario and to inflation expectations are:

upside risks

i. deanchoring of inflation expectations for a longer period;
ii. a stronger-than-expected resilience of services inflation due to a tighter output gap.
iii. a conjunction of external and internal economic policies with inflationary impact, for instance, through an exchange rate persistently depreciated.

downside risks

i. a greater-than-projected deceleration of global economic activity; and
ii. a stronger-than-expected impact on global disinflation from the monetary policy tightening.

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