BANCO CENTRAL DO BRASIL

Minutes of the 190th Meeting of the Monetary Policy Committee (Copom)

Summary
Recent Economic Developments
Assessment of Inflation Trends
Monetary Policy Decision

Date: April 28th, 2015, from 4:19PM to 7:30PM, and April 29th from 4:23PM to 7:40PM

Place: BCB Headquarters meeting rooms – 8th floor on April 28th and 20th floor on April 29th – Brasília – DF

In attendance:
Members of the Committee
Alexandre Antonio Tombini – Governor
Aldo Luiz Mendes
Altamir Lopes
Anthero de Moraes Meirelles
Luiz Awazu Pereira da Silva
Luiz Edson Feltrim
Otávio Ribeiro Damaso
Sidnei Corrêa Marques
Tony Volpon

Department Heads (present on April 28th)
Bruno Walter Coelho Saraiva – International Affairs Department
Eduardo José Araújo Lima – Research Department (also present on April 29th)
Flávio Túlio Vilela – Department of Banking Operations and Payments System
João Henrique de Paula Freitas Simão – Open Market Operations Department
Márcio Barreira de Ayrosa Moreira – Department of Foreign Reserves
Renato Jansson Rosek – Investor Relations and Special Studies Department
Tulio José Lenti Maciel – Economic Department

Other participants (present on April 28th)
Gustavo Paul Kurrle – Press Officer
Maurício Costa de Moura – Chief of Governor's Staff

The members of the Copom analyzed the recent performance and the prospects for the Brazilian economy and for the international economy, under the monetary policy framework, which is designed to comply with the inflation targets established by the government.

Recent Economic Developments

1. Monthly inflation measured by the Extended Consumer Price Index (IPCA) reached 1.32% in March, 0.10 percentage points (p.p.) above the one recorded in the previous month. As a consequence, inflation accumulated in 12 months reached 8.13% in March (6.15% in March 2014). Market prices changed 6.59% (6.99% in March 2014), and regulated prices, 13.37% (3.42% in March 2014). Specifically among market prices, the prices of tradable goods increased 5.68% in twelve months through March (5.71% in March 2014) and the prices of non-tradable goods, 7.40% (8.09% in March 2014). It bears noticing that the prices of the food and beverages group increased 8.19% in in twelve months through March (7.13% in March 2014), and the prices of services rose 8.03% (9.09% in March 2014). In short, available information suggests some persistence of inflation, which partially reflects the dynamics of prices in the services sector and, in the short run, the realignment process of regulated prices.

2. The average of the underlying monthly inflation measures, calculated by the BCB, changed from 0.83% in February to 0.84% in March. As a consequence, on a twelve-month trailing basis, average core inflation

reached 6.96% (0.51 p.p. above the one registered in March 2014). Specifically, the double weight core inflation changed from 0.83% in February to 0.78% in March; the core inflation by exclusion of regulated prices and household food, from 0.91% to 0.57%; and the smoothed trimmed means IPCA core inflation, from 0.77% to 0.76%. On its turn, the non-smoothed trimmed means IPCA core inflation remained at 0.73%, and the core by exclusion, which excludes ten household food items and fuels, changed from 0.90% to 1.34%. The diffusion index stood at 73.5% in March (2.4 p.p. above the one recorded in March 2014).

3. The General Price Index (IGP-DI) increased 1.21% in March, reaching 3.45% on a twelve-month trailing basis (7.55% in March 2014). The main component of this indicator, the Wholesale Price Index (IPA), changed 1.01% in twelve months (8.04% in March 2014), with increases of 2.68% in the prices of agricultural products and 0.34% in the prices of industrial products. Inflation measured by the Consumer Price Index (IPC), the second most important component of the IGP-DI, changed 8.58% in twelve months through March (6.10% in March 2014). The Civil Construction National Index (INCC), component with the lowest weight in the IGP-DI, changed 7.33% (7.81% in March 2014), partially driven by pressures stemming from labor costs, which increased 8.87% in the period. On its turn, the Producer/Manufacturing Industry Price Index (IPP/IT), calculated by the Brazilian Institute of Geography and Statistics (IBGE), increased 0.26% in February, changing 2.74% in twelve months. The Copom considers that the effects of the behavior of wholesale prices on consumer inflation will depend on the current and prospective demand conditions and on the price setters' expectations regarding the future inflation path.

4. The Economic Activity Index of the BCB (IBC-Br) incorporates estimates for the monthly production of the three sectors of the economy, as well as for taxes on products, and constitutes important coincident indicator of the economic activity. In February 2015, the IBC-Br decreased 3.16% year-over-year and increased 0.36% month-on-month, seasonally adjusted. The composite Purchasing Managers' Index (PMI) regarding Brazil changed from 51.3 in February to 47.0 in March, indicating that the private sector output decreased, amid falls, both in the production of manufactured goods and in the services activity. The Industry Confidence Index (ICI), from the Getúlio Vargas Foundation (FGV), decreased 9.2% in March, while the Consumer Confidence Index (ICC) and the Services Confidence Index (ICS) decreased 2.9% and 12.1%, respectively, reaching the record lows for their respective historical series. Regarding agriculture, the Agricultural Production Systematic Assessment (LSPA), carried out by the IBGE in March 2015, indicated that the grains production was expected to grow by 3.6% in 2015, relative to the 2014 harvest.

5. The industrial activity decreased 0.9% in February, after increasing 0.3% in January, according to the seasonally adjusted series released by the IBGE. Therefore, the industrial production accumulates a change of -4.5% in the last twelve months until February. According to the observed series, year-over-year, industrial production decreased 9.1% in February. The result was negative in the four use categories and in 24 out of the 26 surveyed activities, according to the same comparison basis. According to data released by the National Confederation of Industry (CNI), real revenue in the manufacturing industry increased 1.9% between January and February, according to the seasonally adjusted series, and it stood 9.5% lower than the one observed in February 2014. The PMI of the industrial sector, on its turn, decreased from 49.6 in February to 46.2 in March.

6. Among the use categories, according to the February 2015 month-over-month and seasonally adjusted data series, the production of capital goods recorded the most significant decrease (-4.1%), followed by semidurable and non-durable consumer goods (-0.5%), durable consumer goods (-0.4%) and intermediate goods (-0.1%). Regarding year-over-year growth, there was a decrease in the production of the four categories: durable consumer goods (-25.8%), capital goods (-25.7%), semidurable and non-durable consumer goods (-8.9%) and intermediate goods (-4.0%).

7. According to the Continuous National Household Sample Survey (Continuous PNAD), the unemployment rate in the moving quarter ended in February 2015 was estimated at 7.4%, representing an increase of 0.6 p.p. compared to the same quarter of 2014. On its turn, according to the Monthly Employment Survey (PME), covering six metropolitan areas, the unemployment rate reached 6.2% in March. The figure represents increases of 0.3 p.p. compared to February 2015 and of 1.2 p.p. compared to March 2014. Data released by the Ministry of Labor and Employment (MTE) show that 19.3 thousand formal jobs were created in March,

while 50.4 thousand formal jobs were destroyed in the first quarter of this year. In short, the set of available data indicates the beginning of a process of distention in the labor market.

8. According to the retail monthly survey (PMC), released by the IBGE, the retail sales volume decreased 3.1% in February, year-over-year. On its turn, broad retail sales volume, which includes vehicles and construction inputs, fell 10.3% in February, according to the same comparison basis. The month-on-month changes were -0.1% and -1.1%, respectively, according to the seasonally adjusted series. In twelve months, the retail sales growth rate reached 0.9% and the broad retail sales growth stood at -3.8%, with retraction in six out of the ten surveyed segments. The Trade Confidence Index (ICOM), measured by the FGV, underperformed in March, by recording a 4.4% fall month-on-month. The retail sales trajectory will continue to be influenced by the governmental transfers, by the pace of the real payroll growth and by the moderate credit expansion.

9. The installed capacity utilization rate (Nuci) in the manufacturing industry, calculated by the FGV, without seasonal adjustment, reached 79.6% in March and, according to the seasonally adjusted series, 80.4%. Among the industry use categories, according to the seasonally adjusted series, the ones showing the highest Nuci are construction material (85.5%) and intermediate goods (82.8%), followed by non-durable consumer goods (77.5%), capital goods (77.3%) and durable consumer goods (74.6%). On its turn, the absorption of capital goods decreased 13.8% in the last twelve months through February.

10. The twelve-month trailing trade balance deficit reached US$3.4 billion in March 2015. This result stemmed from US$218.3 billion in exports and US$221.7 billion in imports, with retreats of 9.3% and 7.4%, respectively, relative to the cumulative results through March 2014. On its turn, the current account deficit accumulated in twelve months reached US$101.6 billion in March, equivalent to 4.5% of the GDP. Foreign direct investment totaled US$88.8 billion, according to the same comparison basis, equivalent to 4.0% of the GDP.

11. Regarding the global economy, leading indicators signal, in the relevant horizon for monetary policy, growth prospects in line with the trend in important advanced and emerging economies. Particularly about Europe, despite recent monetary policy actions, high unemployment rates, coupled with the fiscal consolidation and political uncertainties, constitute elements constraining investments and growth. Regarding the monetary policy, in general, accommodative stances prevail in advanced and emerging economies. The inflation rates remain at low levels in the advanced economies and at relatively high levels in the emerging ones.

12. The price of the Brent oil barrel has increased since the previous Copom meeting, reaching levels close to US$64. It bears highlighting that the geopolitical complexity that involves the oil sector tends to heighten the volatile behavior of prices. This volatile behavior also reflects the low predictability of some global demand and supply components. Since the last Copom meeting, the international prices of agricultural commodities have retreated 0.78%, while the prices of metal commodities have increased 0.51%. On its turn, the Food Price Index, calculated by the Food and Agriculture Organization of the United Nations (FAO), retreated 18.7% in the twelve months through March 2015.

Assessment of Inflation Trends

13. The identified shocks, and their impacts, were reassessed according to the new set of available information.

14. For the set of regulated prices, the projected inflation for 2015 stands at 11.8%, up from 10.7% considered at the March Copom meeting. Among other factors, this projection considers the assumption of changes of 9.8% in the price of gasoline and 1.9% in the price of bottled gas; of -4.1% in fixed telephone tariffs; and of 38.3% in electricity prices. The items for which there is more information available were projected individually. For the others, the projections are based on endogenous determination models for regulated prices, which compute, among other factors, seasonal components, market prices inflation and the IGP (General Price Index) change. Based on these models, the projected regulated prices change is 5.3% for 2016, up from 5.2% considered at the March meeting.

15. On the baseline cenario, the estimated path for the spreads over the Selic rate, based on the 360-day swap rates, is -1 basis points (bps) and +14 bps for the fourth quarters of 2015 and 2016, respectively.

16. The structural primary surplus is considered as the fiscal indicator. It derives from the primary surplus trajectories set at R$ 66.3 billions in 2015 and 2% of the GDP in 2016, respectively. It also bears emphasizing that, in a given period, the fiscal impulse is equivalent to the change of the structural surplus compared to the observed in the previous period.

17. Since the last Copom meeting, the median of the projections compiled by the Investor Relations and Special Studies Department (Gerin) for the 2015 IPCA has changed from 7.47% to 8.25% and, for 2016, from 5.50% to 5.60%.

18. The baseline scenario assumes the maintenance of the exchange rate at R$3.00/US$1.00 and the Selic rate at 12.75% p.a. during the forecast period. Under this scenario, the projection for the 2015 inflation remained stable compared to the value considered at the previous Copom meeting and remains above the 4.5% target established by the National Monetary Council (CMN). In the the market scenario, which incorporates the market expectations for the exchange and Selic rates trajectories collected by Gerin, in the period immediately prior to the Copom meeting, the 2015 IPCA inflation forecast also remained close to the value considered at the March meeting and remains above the inflation target. For 2016, according to the baseline scenario, the inflation forecast remained stable, but increased in the market scenario. In both scenarios, it remains above the 4.5% target established by the CMN.

Monetary Policy Decision

19. The Copom emphasizes that the international evidence, which is ratified by the Brazilian experience, indicates that high inflation rates generate distortions that lead to higher risks and depress investments. These distortions are manifested, for example, in the shortening of the planning horizons of households, companies and governments, as well as in the deterioration of the businessmen confidence. The Committee also emphasizes that high inflation rates reduce the purchasing power of wages and transfers, with negative repercussions over households' confidence and consumption. As a consequence, high inflation rates reduce the potential of economic growth, as well as of jobs and income generation.

20. In this context, the Copom evaluates that the monetary policy should contribute to the consolidation of a favorable longer-term macroeconomic environment. In this respect, the Copom reassures that, under the inflation targeting regime, it guides its decisions according to BCB projected inflation and based on the analysis of alternative scenarios for the evolution of the main variables that determine prices dynamics. The Committee also understands that low risks for the underlying inflation in the short run tend to reduce uncertainties regarding the future behavior of headline inflation, facilitate the assessment of scenarios by the monetary authority, as well as help the process of coordination of economic agents' expectations, particularly prices setters'. Additionally, it is noteworthy that low risks for the underlying inflation in the short run tend to intensify the effects of monetary policy actions, enabling them to affect, in a more long-lasting manner, the dynamics of headline inflation in the future. Although the Copom recognizes that other macroeconomic policy actions may influence the prices trajectory, it reaffirms its view that it is particularly under the responsibility of the monetary policy to remain especially vigilant, to guarantee that pressures detected in shorter horizons do not spread to longer horizons.

21. The Copom considers that, since its last meeting, the risks to global financial stability have remained high, such as those derived from changes in the yield curve slope of major advanced economies. Despite identifying low probability of occurrence of extreme events in the international financial markets, the Committee considers that the external environment remains complex. For the Committee, a more intense global activity trend prevails throughout the monetary policy relevant horizon. In this respect, the prospects indicate activity recovery in some advanced economies and acceleration in the pace of growth in others, although, in general, the room to use monetary policy in these economies remains limited and a fiscal restraint scenario prevails. Important emerging economies experience a transition period, and therefore, of moderation in the activity pace, despite the resilience of the domestic demand.

22. Still regarding international financial markets, the Copom highlights evidence of volatility sources in the currency markets and moderation in the dynamics of commodities prices. Regarding oil, the Committee highlights that, regardless of the behavior of the domestic prices of gasoline, the evolution of international prices tends to be transmitted to the domestic economy both through productive chains, such as the petrochemical, and through inflation expectations.

23. The Copom notices that the available indicators regarding domestic absorption and GDP growth rates have converged and that the domestic activity expansion pace this year will be lower than the potential. In particular, the investment has retreated, mainly influenced by the occurrence of non-economic events. However, for the Committee, after a necessary period of adjustments, the activity expansion pace tends to intensify, as companies' and households' confidence strengthen. Moreover, the Committee evaluates that, in the medium term, important changes should take place in the composition of aggregate supply and demand. The consumption tends to grow at a moderate pace and the investments tend to gain momentum. These changes, together with other currently underway, anticipate a composition for medium-term aggregate demand growth more favorable to potential growth. Regarding the external component of aggregate demand, the scenario of higher global growth, combined with the depreciation of the BRL, contributes to make this component more favorable to the Brazilian economy growth. Regarding the supply side, the Committee evaluates that, in longer terms, more favorable prospects for the competitiveness of industry and agriculture have emerged. The services sector, on its turn, tends to grow at rates lower than those recorded over the recent years. For the Committee, it is plausible to claim that these developments – coupled with advances in terms of qualification of the labor force and with the program of public services concession - will be reflected in a more efficient allocation of the production factors of the economy and in productivity gains.

24. The Copom observes that the main inflation scenario considers the materialization of the assumed trajectories regarding fiscal variables. The Committee argues that, during the relevant horizon for the monetary policy, the balance of the public sector tends to shift to the neutral zone, and does not rule out the hypothesis of migration to the fiscal restraint area. The Committee also notes that the generation of primary surpluses in line with the working hypotheses considered in the inflation projections will contribute to create a positive perception regarding the macroeconomic environment in the medium and long terms. It also highlights that this primary surpluses' path will strengthen the perception of sustainability of the public sector balance. Thus, it contributes to reduce the public debt financing cost, with favorable impact on the cost of capital in general, stimulating private investment in the medium and long terms. Specifically regarding inflation control, the Committee highlights that the literature and the best international practices recommend a consistent and sustainable fiscal policy, in order to allow monetary policy actions to be fully transmitted to prices.

25. The Copom highlights that the main scenario also considers moderate credit expansion, which is already being observed. It's important to highlight the fact that, after years of strong expansion, the consumer credit has moderated, so that, over the last quarters, it was possible to observe, on the one hand, exposure reduction by banks, and, on the other hand, deleveraging of the households. In the aggregate, therefore, it can be inferred that the risks in the consumer credit segment have been mitigated. In another dimension, as illustrated by the recently implemented actions, the Committee considers as necessary the initiatives with the aim of moderating concessions of subsidies through credit operations.

26. Regarding the factors' market, as anticipated by previous Minutes, the Copom highlights that the narrow idleness margin in the labor market has eased at the margin, with some data indicating the start of a process of distension in this market. However, the Copom notices that it is necessary to broaden the horizon of observations, and that a significant risk still prevails related, particularly, to the possibility of concession of wages increases incompatible with productivity growth, with negative impacts over inflation. In spite of the concession of adjustments for the minimum wage not so significant, and the occurrence of real wage changes more consistent with the gains estimated for the labor productivity, the Committee evaluates that the wages dynamics remains originating inflationary cost pressures.

27. For the Copom, the fact that inflation currently stands at high levels reflects, in large part, the occurrence of two important relative prices adjustment processes underway in the economy - the realignment of domestic

prices relative to international prices and the realignment of regulated prices relative to market prices. The Committee also considers that, since its last meeting, these relative prices ajustments in the economy, among other factors, have made the balance of risks to inflation unfavorable this year. In this context, and as anticipated in previous Minutes, these price adjustments cause inflation to rise in the short term and to tend to remain high in 2015. While recognizing that these relative prices adjustments have direct impacts on inflation, the Committee reaffirms its view that monetary policy can and should contain the second order effects arising from them, in order to limit them to 2015.

28. Given the above, assessing the macroeconomic scenario and the inflation prospects, the Committee unanimously decided to raise the Selic rate by 0.50 pp, to 13.25% p.a., without bias.

29. The following members of the Committee voted for this decision: Alexandre Antonio Tombini (Goveror), Aldo Luiz Mendes, Altamir Lopes, Anthero de Moraes Meirelles, Luiz Awazu Pereira da Silva, Luiz Edson Feltrim, Otávio Ribeiro Damaso, Sidnei Corrêa Marques and Tony Volpon.

30. The Copom evaluates that the aggregate demand tends to be moderate in the relevant horizon for the monetary policy. On the one hand, household consumption tends to stabilize, due to factors such as employment, income and credit; on the other hand, the real state financing, the concession of public services and the expansion of agricultural income, among other factors, tend to benefit investments. On its turn, exports tend to be benefited by the scenario of higher growth of major trading partners and by the depreciation of the real. For the Committee, the combined effects of these elements, and the developments in the quasi fiscal framework and in the assets market and, this year, the dynamics of recovery of regulated prices are important factors in the context in which future monetary policy decisions will be taken, aiming to ensure the convergence of inflation to the 4.5% target established by CMN, at the end of 2016.

31. Accordingly, the Copom believes that the convergence scenario of inflation to 4.5% at the end of 2016 has strengthened. For the Committee, however, the progress made in the fight against inflation - like benign signals stemming from the medium and long term expectations indicators – has not been sufficient yet. In this context, the Copom reaffirms that the monetary policy should remain vigilant.

32. At the end of the meeting, it was announced that the Committee will reconvene on June 2nd 2015, for the technical presentations, and on the following day, to deliberate on monetary policy, as established in the Communiqué 26,042, of June 24th, 2014.