



BANCO CENTRAL DO BRASIL

Translation of the Open Letter sent by the Governor of the Banco Central do Brasil, Gabriel Muricca Galípolo, to the President of the National Monetary Council, Fernando Haddad*

Notice 374/2025–BCB/Gapre

Brasília, January 10, 2025.

Mr.
Fernando Haddad
Minister of Finance
President of the National Monetary Council

Subject: Open letter explaining inflation above the upper limit of the target tolerance interval in 2024

Dear Mr. Haddad,

The “inflation-targeting regime” was created as a monetary policy framework by means of Decree 3,088 of June 21, 1999. Currently, the regime is ruled by Decree 12,079 of June 26, 2024. Nevertheless, Article 7 of Decree 12,079 of 2024 established that, for the purposes of the target and tolerance interval set by the National Monetary Council (CMN) for 2024 and for the assessment of its compliance and the measures to be adopted in the event of target breach, the provisions of Decree 3,088 of 1999 shall be observed. In its sole paragraph of article 4, the decree establishes that when year-over-year (YoY) inflation falls outside the tolerance interval at the end of a given calendar year,

“the Governor of the Banco Central do Brasil (BCB) shall disclose the reasons for the breach of the inflation target by means of an open letter addressed to the Minister of Finance, which shall contain:

I - a detailed description of the causes for the target breach;

II - the measures to ensure the return of inflation to the established limits; and

III - the expected time span for the measures to take effect.”

2. **In 2024, the inflation rate, measured by the change of the Extended National Consumer Price Index (IPCA), reached 4.83%, above the upper limit of the tolerance interval of 4.50%.** The upper limit set by the CMN by means of Resolution 4,918 of June 24, 2021, corresponds to the inflation target of 3.00% plus 1.50 percentage points (p.p.). Therefore, pursuant to the sole paragraph of Article 4 of Decree 3,088 of 1999, I hereby submit this open letter.

***In case of any inconsistency, the original version in Portuguese prevails.**

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



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I. Causes of inflation exceeding the upper limit of the tolerance interval of the target in 2024

3. **Inflation in 2024 was above the tolerance interval due to the strong pace of economic activity growth, the exchange rate depreciation, and climate factors, in a context of deanchored inflation expectations and inertia from the previous year's inflation.** Therefore, inflation involved a wide group of factors. In the opposite direction, it was notable the oil price decline in the second half of the year.

4. **The inflationary pressure affected different IPCA segments, reflecting the variety of inflationary drivers** (Table 1 and Figure 1). In 2023, the inflation rate was similar, 4.62%, but with a highly heterogeneous behavior across segments, with more pressures in services and administered prices.¹ In 2024, market and administered prices grew 4.89% and 4.66%, respectively, highlighting:

- **Food-at-home** – after a deflation of -0.52% in 2023, food-at-home reached 8.22% in 2024, reflecting climate factors, basically related to the drought that affected a great extent of the country, the cattle cycle, and the exchange rate depreciation, combined with pressures from economic activity and an increase of international prices of some agricultural commodities. Within this segment, the largest increase occurred in semi-processed food (14.93%), especially the rise of beef prices (20.84%);
- **Industrial goods** – industrial goods inflation also increased, from 1.10% in 2023 to 2.89% in 2024. The rise reflected the exchange rate depreciation, the higher international price of metal commodities, and the expansion of economic activity;
- **Services** – Services inflation fell in relation to 2023, from 6.22% to 4.77%. Excluding airfares, inflation in this segment rose from 5.40% to 5.53%. Services inflation was particularly pressured by inertial factors and the economic activity; and
- **Administered** – The largest contribution in this segment came from the rise of gasoline prices (9.70%). Despite the drop in international oil prices, which would favor lower domestic gasoline prices, there was a significant BRL depreciation, a rise in anhydrous ethanol prices, and an increase in the *ad rem* rates of the State Value-Added Tax on Sales and Services (ICMS) on fuels, effective from February 2024. It should also be mentioned the inflation rates of health insurance (7.88%) and pharmaceutical goods (5.96%).

¹ For further details, see the box “Breakdown of 2023 inflation”, in the March 2024 Inflation Report (IR).

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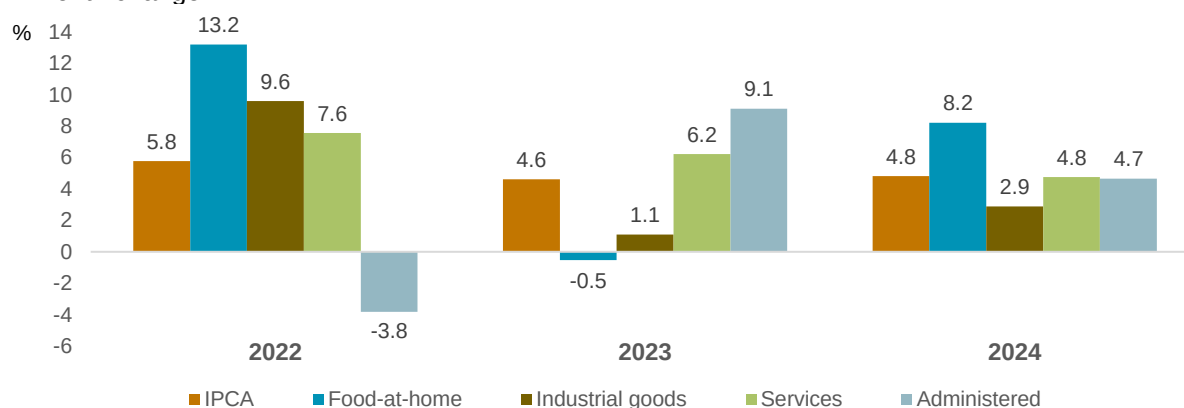
SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br

Table 1 – Selected components of the IPCA in 2024

Selected components and items	Change (%)	Weight	Contribution to IPCA change (p.p.)
Market prices	4.89	74.14	3.62
Food-at-home	8.22	15.26	1.26
Industrial goods	2.89	23.35	0.67
Services	4.77	35.52	1.70
Administered prices	4.66	25.86	1.21
Consumer Inflation (IPCA)	4.83	100.00	4.83

Sources: IBGE and BCB

Figure 1 – IPCA inflation and components
12-month change



Sources: IBGE and BCB

5. **The role of inflation drivers can be quantitatively assessed through macroeconomic models.** Using semi-structural BCB models², the contributions – whether positive or negative – of the following factors underlying the inflation deviation from the target are identified: (i) inertia associated with the deviation of previous year’s inflation from the target; (ii) deviations of agents’ inflation expectations – measured by the BCB’s Focus survey – from the inflation target; (iii) imported inflation (combination of changes in the exchange rate and in commodity prices – including oil) as deviation from the target; (iv) output gap; and (v) other factors. The latter item includes factors not considered in the previous ones – mainly specific factors conditioning administered prices, the effect of climate anomalies and tax measures – and a part not explained by the model (shocks in the Phillips curve of market prices and in the equations of administered prices).³ It is worth noting that these estimates are based on models and, therefore, are

² In particular, see the box “Revision of the small-scale aggregate model”, in the December 2024 IR.

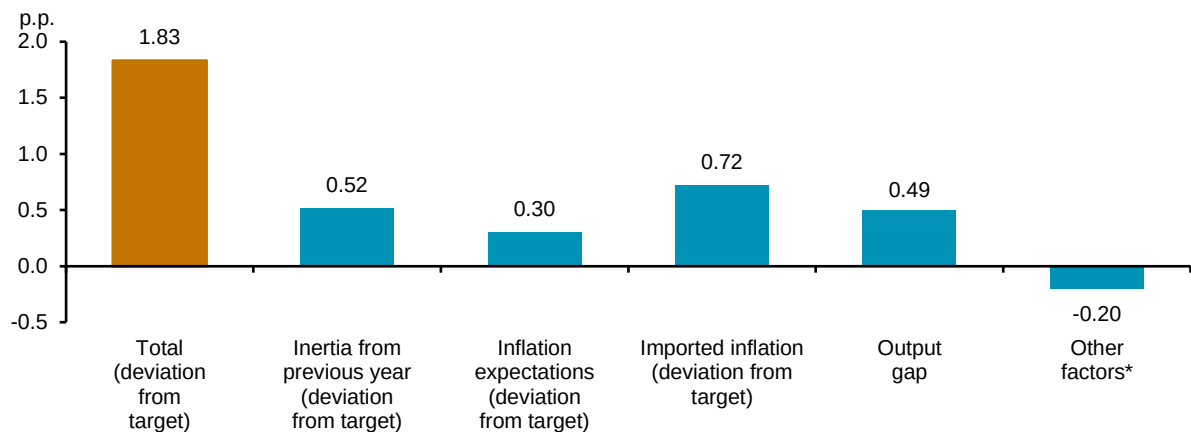
³ Further details on methodological procedures are available in the box “2017 inflation decomposition”, in the March 2018 IR, and CUSINATO, R. T., FIGUEIREDO, F. M. R., MACHADO, V. G., MELLO, E. P. G. and PEREZ, L. P. (2016), “Decomposição de Inflação: revisão da metodologia e resultados para 2012 a 2014”, Banco Central do Brasil, Working Paper 440. The results using this methodology are usually presented in the March IR of each year.

subject to uncertainties inherent to the modeling and estimation processes. The contributions presented below were calculated by the small-scale aggregate semi-structural model.

6. **The main factors that contributed to the 1.83 p.p. inflation deviation from the target were imported inflation (contribution of 0.72 p.p.), the inertia from the previous year (0.52 p.p.), the output gap (0.49 p.p.), and inflation expectations (0.30 p.p.)** (Figure 2). Within the imported inflation group, the main contribution came from the exchange rate depreciation (a 1.21 p.p. effect)⁴, followed by commodities in general, measured by the Commodities Index – Brazil (IC-Br) (a 0.10 p.p. effect), which more than offset the estimated effects of the international oil price decline (a -0.59 p.p. effect).

Figure 2 – Contributions to the deviation of inflation from target in 2024

Contribution from factors



* Contribution to the inflation as deviation from the target after excluding the following factors: inertia associated with the portion of the previous year's inflation that deviated from target; expectations as a deviation from target; imported inflation as a deviation from target; and output gap.

Source: BCB

7. **The significant BRL depreciation was mainly due to domestic factors, coupled with the global USD appreciation.** The exchange rate increased from an average of USD/BRL 4.95 in 2023Q4 to USD/BRL 5.84 in 2024Q4, representing a 18.0% change (Figure 3). Considering the average in December 2023 and December 2024, the exchange rate rose from USD/BRL 4.90 to USD/BRL 6.10, a 24.5% change, corresponding to a BRL depreciation of 19.7%. The depreciation process started in April 2024 and intensified throughout the year. Therefore, part of the direct and indirect effects of the exchange rate pass-through is still expected to materialize in 2025. The global USD appreciation was mainly driven by a slower-than-expected decline in the Fed Funds Rate and the prospect of changes in the U.S. economic policy as a result of the U.S. election outcome. However, the fact that the BRL was the mostly depreciated currency compared with its international peers and advanced countries (Figure 4) suggests that domestic and specific factors in Brazil played a significant role in this exchange rate movement. Domestically, the perception of agents about the fiscal scenario has significantly impacted asset prices and expectations, especially the risk premium,

⁴ The contribution of the exchange rate change is calculated considering its deviation in relation to the 1% change, corresponding to the difference between the Brazilian inflation target of 3% p.a. and the long-term external inflation rate, considered to be 2% p.a., in line with the inflation target of most developed countries.

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



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inflation expectations, and the exchange rate. The terms of trade did not play a significant role, as, after worsening for a few months in 2024, they soon recovered, reaching levels in the second half of the year close to those at the same period of 2023.

Figure 3 – Exchange rate

Monthly average

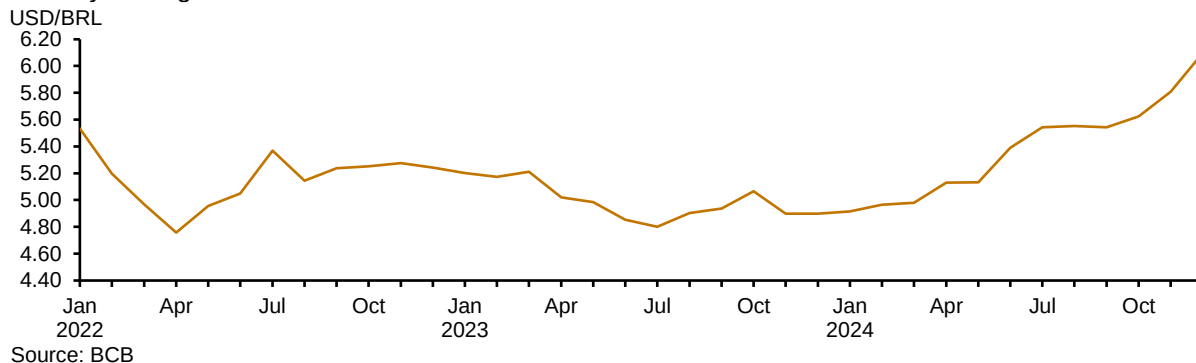
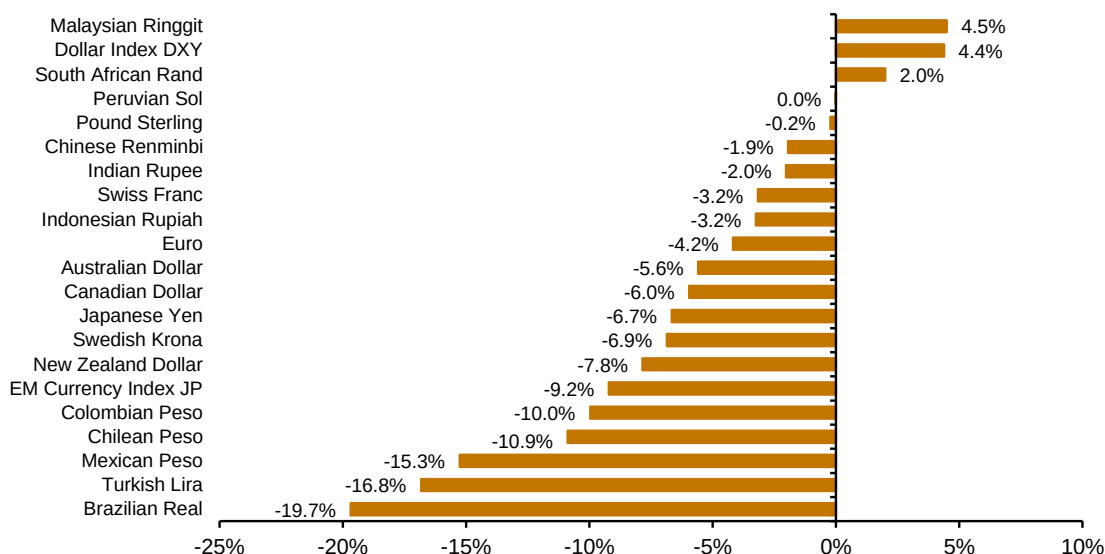


Figure 4 – Change in currency values with respect to USD in 2024



Note: Change between Dec. 2023 and Dec. 2024 averages. The US Dollar Index DXY refers to the USD value relative to a basket of currencies from selected countries.

Source: Bloomberg

8. **Conversely, the drop in international oil prices cushioned the impact of the exchange rate depreciation.** The price of the Brent-type oil, after rising until April, followed a downward trend, reaching an average of USD 73.13 per barrel in December 2024, a reduction of 5.4% compared with USD 77.32 per barrel in December 2023 (Figure 5). This reduction reflected smaller-than-expected global demand and larger-than-expected supply growth. However, when measured in BRL, the price increased 15.1%, reflecting the greater magnitude of the exchange rate depreciation in relation to the international oil price decline. Agricultural commodity prices fluctuated throughout the year, but increased in recent months, leading to a 13.5% rise in the year,

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



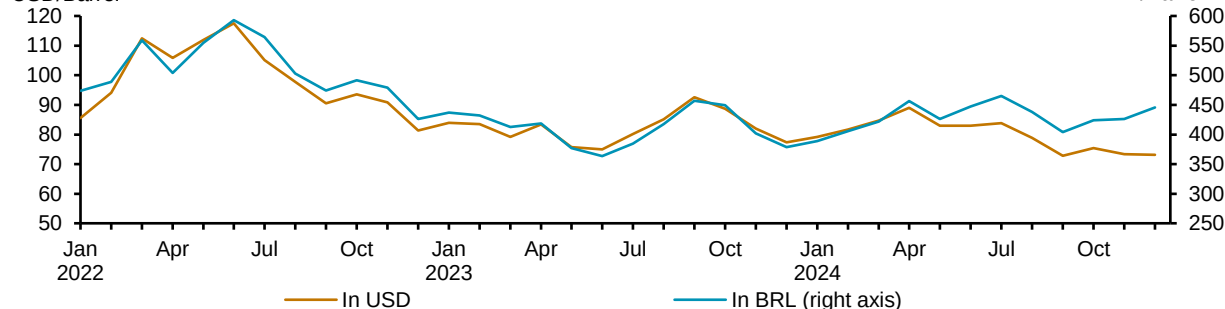
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comparing the December IC-BR Agriculture average measured in USD with the average of the same month in 2023. On the same basis of comparison, the IC-BR Metal measured in USD rose 15.9%, mainly impacting industrial goods. Considering the IC-Br (aggregate), there was also an increase in the index measured in USD and an even stronger increase when measured in BRL (Figure 6).

Figure 5 – Brent oil price

Monthly average

USD/Barrel

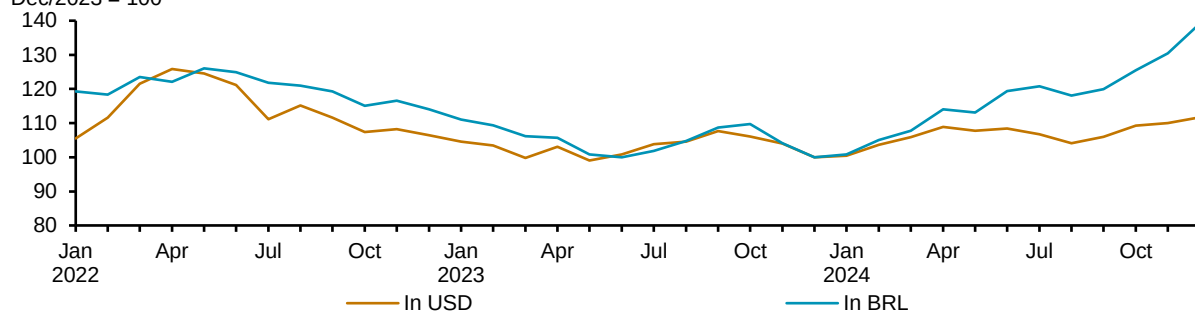


Sources: Bloomberg and BCB

Figure 6 – IC-Br

Monthly average

Dec/2023 = 100



Source: BCB

9. **Economic activity growth, which exceeded expectations throughout 2024, was strong and contributed to inflation above the tolerance interval.** As of 2024Q3, Gross Domestic Product (GDP) growth in the year to date was 3.3% compared with the same period in 2023. The BCB projects a GDP growth of 3.5% in 2024. A significant expansion in domestic demand stands out, particularly household consumption and Gross Fixed Capital Formation (FBCF), which grew 5.1% and 6.6%, respectively, on the same basis of comparison. Consumption growth reflected the increase in the real wage bill, the rise in government transfers, and the expansion of credit. In the QoQ comparison, average seasonally adjusted GDP growth rates reached 1.1% in the first three quarters of 2024, equivalent to 4.5% in annualized terms (Figure 7). This dynamism was reflected in the output gap estimate, which, after remaining around relatively neutral values in 2023 (average of 0.1%), increased to an average of 0.6% in 2024 (0.7% in 2024Q4). This economic activity performance was well above the expectations of the BCB and analysts. From the December 2023 to the December 2024 Inflation Reports, the growth forecast for 2024 was revised from 1.7% to 1.9%, 2.3%, and 3.2%, reaching 3.5% in the most recent IR. The Focus survey expectations, which estimated a 1.5% growth on December 8, 2023, also underwent a similar revision process.

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br

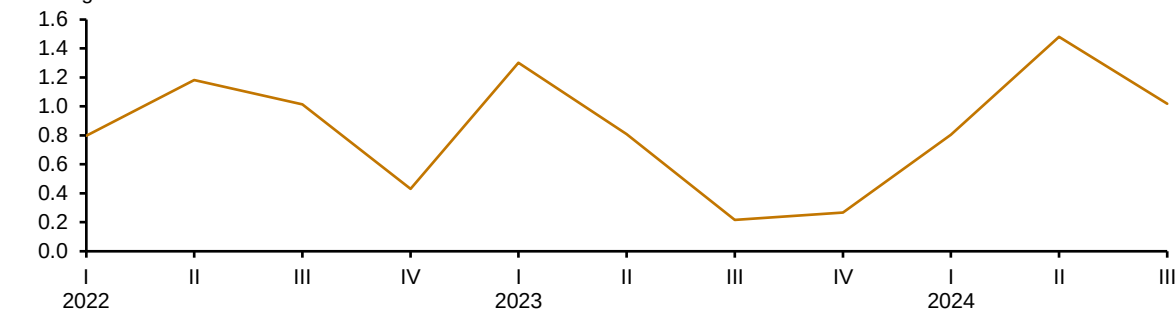


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Figure 7 – Gross Domestic Product

QoQ, s.a.

% change



Source: IBGE

10. **The slack of production factors decreased, highlighting the historical low reached by the unemployment rate.** The labor market achieved robust results in 2024. The unemployment rate continued to decline rapidly, reaching 6.5% in November (seasonally adjusted), the lowest value in the time series (Figure 8). On a YoY comparison, the non-seasonally adjusted rate dropped from 7.5% in November 2023 to 6.1% in November 2024. The low unemployment rate was accompanied by an increase in wages. The average nominal income usually received by all workers from January and November 2024 was 9.0% higher than in the same period of 2023, corresponding to an increase of 4.5% in real terms. Net hirings measured by the New General Registry of Employed and Unemployed Persons (Novo Caged) indicated 1.8 million jobs created in twelve months up to November⁵ (Figure 9). Although at a slower pace than in early 2024, seasonally adjusted monthly net hiring has been robust, ranging from 100 to 150 thousand between May and November. Other indicators also point to a heated labor market, such as the hiring-to-layoff salary ratio at historically high levels and the percentage of voluntary resignations at its historical maximum. Increased use of capital was also observed. The Industry Installed Capacity Usage Level (Nuci), calculated by Getulio Vargas Foundation (FGV) with seasonally adjusted data, rose from 81.1% in December 2023 to a peak of 83.4% in July and September 2024, the highest level since May 2011. Despite reducing in the following months, reaching 81.1% in December, the Nuci remains at a historically high level.

⁵ Data do not consider information from late statements.

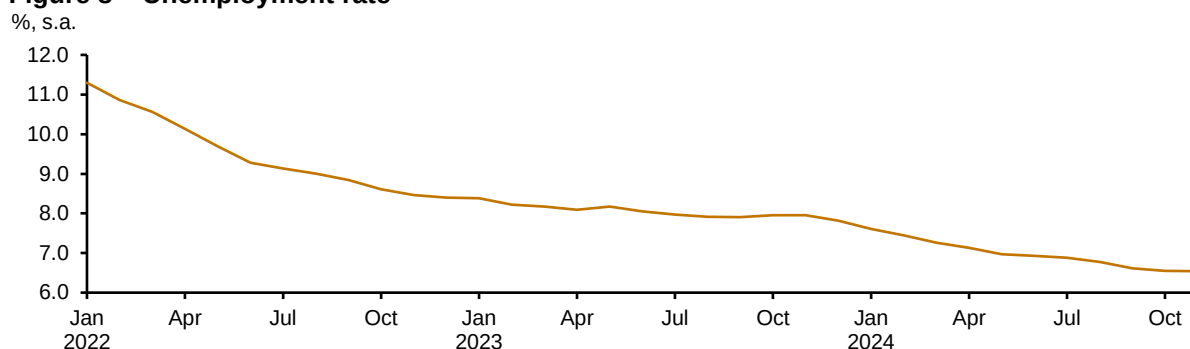
Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



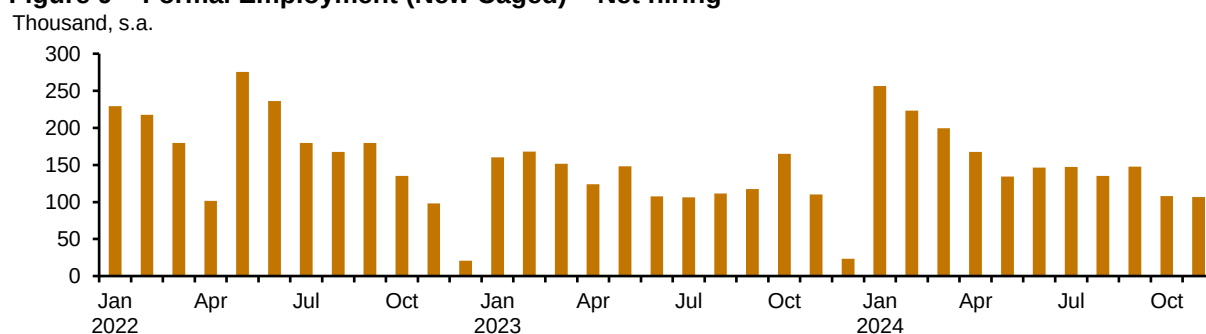
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Figure 8 – Unemployment rate



Sources: IBGE and BCB

Figure 9 – Formal Employment (New Caged) – Net hiring



Sources: MTE and BCB

11. **Inflationary inertia also impacted inflation in 2024.** Inflation in 2023 was 4.62%, 1.37 p.p. above the target. In the case of market prices, past inflation means current costs pressure, arising from both other prices of goods and services used as inputs and informal inertial mechanisms of wage indexation. For example, adjustments in wage negotiations not only followed the past inflation trend but were also above inflation. Regarding administered prices, it is noteworthy the institutional arrangements linking the adjustment of prices to past inflation, especially for health insurance and medicines.⁶

12. **The effects of the drought and the cattle cycle also contributed to inflation.** The drought that affected a great extent of the country pressured food prices – especially beef and milk, due to pasture deterioration – and such products as coffee and orange. The cattle cycle impacted beef prices significantly and more strongly than expected, adding to the effects of the drought and the exchange rate depreciation. In 2024Q2, floods in Rio Grande do Sul impacted some food prices, especially in this federation unit, but in general there was a reversal in the subsequent months. Using the disaggregate small-scale model, it is estimated that the effects of the climate anomaly measured by the temperature of the Pacific Ocean and the shocks to the Phillips curve of food-at-home prices contributed jointly with 2.43 p.p. to its respective inflation, corresponding to a direct impact of 0.38

⁶ The small-scale semi-structural model captures this effect through terms related to both the 12-month inflation and the market prices inflation in the previous quarter. Regarding administered prices, inertia depends on each item. See box “Reformulation of models for administered prices – medium term projection” in the September 2017 IR.

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br

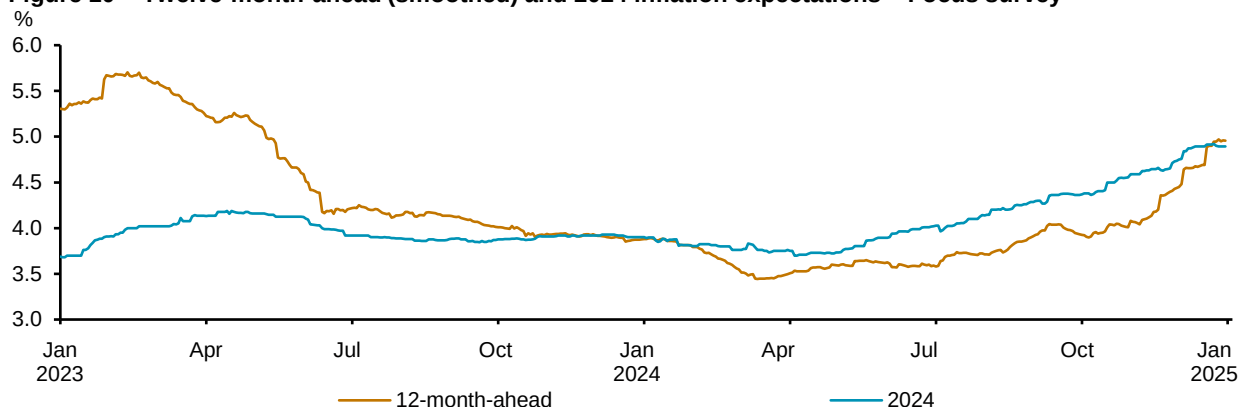


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p.p. on the IPCA change in 2024. In contrast, the improvement in rainfall in the last months of 2024 meant that the green electricity tariff flag – the same as in December 2023 – was maintained until the end of 2024, so that inflation in this year was not directly affected by this factor. The red 1 electricity tariff flag had been triggered in September 2024, and the red 2 flag in October, but in November the tariff flag was reduced to yellow and, in December, to green.

13. **Inflation expectations deteriorated throughout 2024, both for shorter and longer horizons, thus increasing their deanchoring.** The rise in expectations reflected current and prospective inflationary pressures. According to the Focus survey, the median expectations for the 12-month-ahead inflation (smoothed), measure used by the aforementioned semi-structural models, started 2024 around 3.9% and declined until early May, when it reached 3.6%. It remained around this value until early July, when began a rapid upward trajectory, ending the year around 5.0% (Figure 10). The median expectations for 2024 followed a similar behavior. It started around 3.9%, fell until April, reaching 3.7%, but then began an upward trajectory, surpassing the upper limit of the tolerance interval of 4.50% in October. For longer horizons, such as 2025, 2026, and 2027, starting from 3.50% in early 2024 for each of these three years, the median on January 3, 2025 was 5.0%, 4.0%, and 3.9%, respectively.

Figure 10 – Twelve-month-ahead (smoothed) and 2024 inflation expectations – Focus survey



Note: The figure data range is 1/2/2023 – 1/3/2025

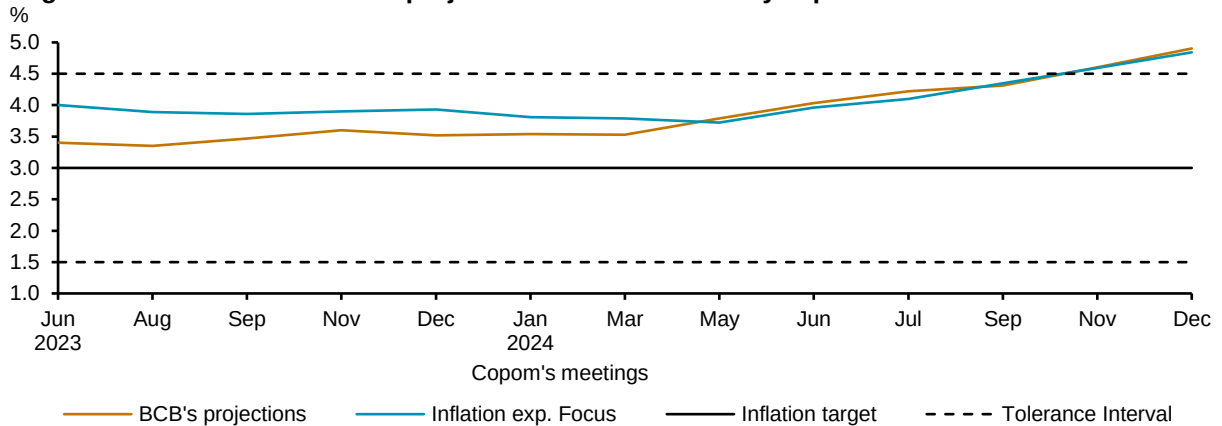
Source: BCB

14. **The analysis of BCB's conditional projections for inflation over 2024 corroborates the worsening of the inflationary factors throughout the year.** BCB's conditional projections for inflation in 2024 ranged between 3.4% and 3.6% in the Copom meetings from June 2023 to March 2024 (Figure 11). However, starting in the May meeting, projections began to rise. The increase in inflation projections was mainly due to the sequence of exchange rate depreciations, positive economic activity and labor market surprises, and the rise in inflation expectations throughout the period. In the last months of the year, it also reflected surprises in food-at-home prices. A similar movement occurred with expectations from the Focus survey. Conversely, the movement that started in 2024Q2, of increased Selic rate expectations for the next four quarters from the Focus survey, helped to prevent a sharper increase in projections.

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br

Figure 11 – Evolution of BCB's projections and Focus survey expectations for 2024 inflation



Note: Focus' expectations are collected on the Friday prior to the Copom meeting.
Source: BCB

II Measures to ensure the return of inflation to the established limits

15. **The BCB has set the Selic rate target to ensure the convergence of inflation to the target.** After a period of monetary easing, Copom resumed the interest rate hike cycle with adjustments of increased magnitude, and signalization, in the December meeting, of the steps for the subsequent two meetings.

16. **In August 2023, due to an improved inflation scenario, the BCB began a monetary easing process that lasted until May 2024.** The Selic rate was reduced from 13.75% p.a. to 10.50% (Table 2 and Figure 12). Considering the relevant monetary policy horizon, the conditional projections for six-quarter-ahead inflation, after peaking at 3.8% in the March 2023 IR, fell in the subsequent IRs, standing at 3.1% in the December 2023 and March 2024 IRs (Figure 13). The projections considered economic deceleration ahead. Indeed, QoQ GDP grew 0.2% in 2023Q3 and 2023Q4. In the September 2023 IR, the estimated output gap for 2023Q3 was -0.7%, and the projection for 2024Q4 was -0.8%.

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



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Table 2 – Copom's decisions

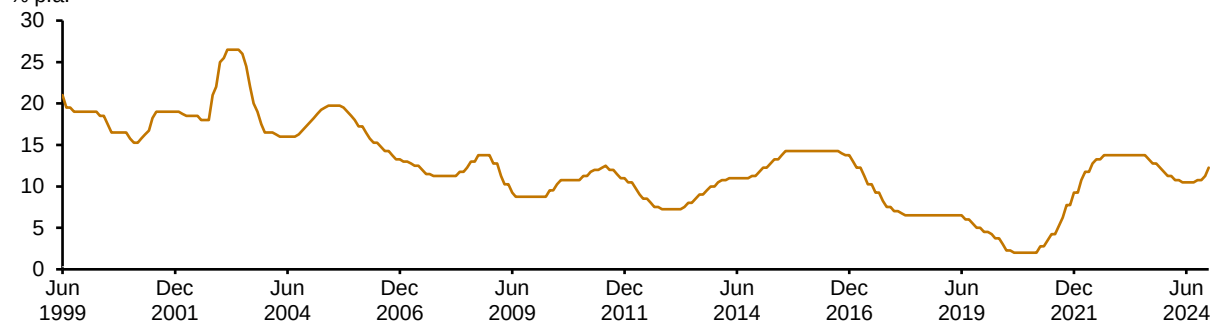
Meeting	Decision's date	Selic rate (% p.a.)	Change (p.p.)
252 nd	02/01/2023	13.75	0.00
253 rd	03/22/2023	13.75	0.00
254 th	05/03/2023	13.75	0.00
255 th	06/21/2023	13.75	0.00
256 th	08/02/2023	13.25	-0.50
257 th	09/20/2023	12.75	-0.50
258 th	11/01/2023	12.25	-0.50
259 th	12/13/2023	11.75	-0.50
260 th	01/31/2024	11.25	-0.50
261 st	03/20/2024	10.75	-0.50
262 nd	05/08/2024	10.50	-0.25
263 rd	06/19/2024	10.50	0.00
264 th	07/31/2024	10.50	0.00
265 th	09/18/2024	10.75	0.25
266 th	11/06/2024	11.25	0.50
267 th	12/11/2024	12.25	1.00

Source: BCB

Figure 12 – Selic rate target

End of month

% p.a.

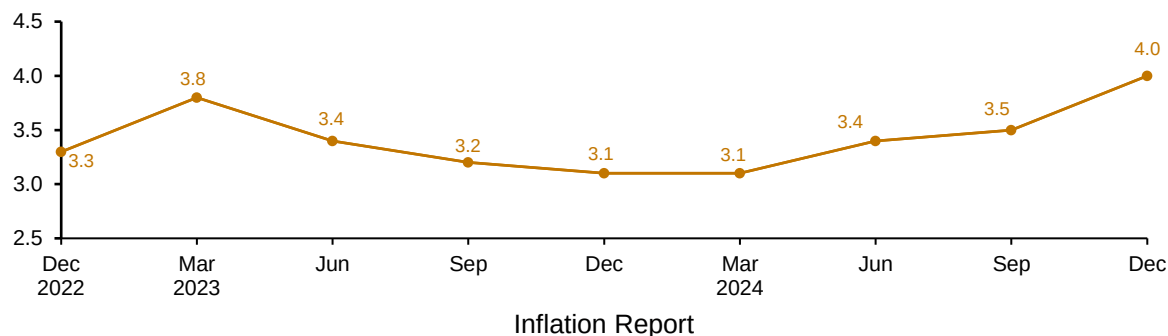


Source: BCB

Figure 13 – Evolution of six-quarter-ahead inflation projections

YoY IPCA inflation

%



Source: BCB

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



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17. **However, due to the worsening of the prospective scenario, Copom maintained the Selic rate at 10.50% in the June and July meetings.** In the June meeting, Copom highlighted the increase in inflation projections, the continuity of greater-than-expected dynamism in economic activity and labor market, and the further deanchoring of inflation expectations. The communication also emphasized the need for a contractionary monetary policy for enough time at a level that would consolidate not only the disinflationary process but also the anchoring of inflation expectations around its targets. The need for vigilance was also highlighted. In the July meeting, Copom expanded the list of upside risks to inflation, highlighting the more prolonged period of deanchoring of inflation expectations and the conjunction of external and internal economic policies with an inflationary impact. The Committee emphasized that the domestic and international scenarios still required more caution in the conduct of monetary policy. In particular, it was stressed that inflationary impacts stemming from market variable movements and inflation expectations, if persistent, would support the need for greater vigilance. The worsening of economic agents' perception about the fiscal scenario and its impact on asset prices and agent expectations was also mentioned. The Committee also emphasized that the uncertain global scenario and the domestic situation marked by activity resilience, higher inflation projections, and deanchored expectations required diligent monitoring and even greater caution.

18. **In the September meeting, Copom began a tightening monetary cycle, raising the Selic rate by 0.25 p.p. to 10.75%, considering that the scenario required an even more contractionary monetary policy.** The scenario was characterized by resilience in activity, pressures in the labor market, positive output gap, higher inflation projections, and deanchored inflation expectations. In its analysis, the Committee highlighted that the greater-than-expected dynamism in economic activity and labor market led to a reassessment of the output gap as positive. As for when to start the cycle, the Committee believed that it should be gradual, so as to, on the one hand, benefit from closely monitoring the data, especially in the context of uncertainties in both external and domestic scenarios, but on the other hand, allow the transmission mechanisms of monetary policy that would enable inflation to converge to the target to begin to operate. The total magnitude of the tightening cycle would be determined by the firm commitment of reaching the inflation target and would depend on the inflation dynamics, especially the components that are more sensitive to economic activity and monetary policy, on the inflation projections, on the inflation expectations, on the output gap, and on the balance of risks. Due to the uncertainties involved, the Committee preferred a communication that emphasized the importance of monitoring scenarios over time, without providing any future indication of its next steps, while insisting on its firm commitment to reaching the inflation target.

19. **In the November meeting, considering the need for a more contractionary monetary policy, the Committee deemed it appropriate to increase the Selic rate by a larger amount of 0.50 p.p. to 11.25%.** The Committee considered the increase of this magnitude appropriate, given the current economic conditions and prospective uncertainties, reflecting the commitment of reaching the inflation target, which is essential to the continuous construction of credibility.

20. **In its latest meeting in December, Copom increased the Selic rate by 1.00 p.p. to 12.25%, considering that the more recent scenario, marked by additional deanchoring of inflation expectations, higher inflation projections, greater-than-expected dynamism in**

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



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activity, and a widening output gap, required an even more contractionary monetary policy.

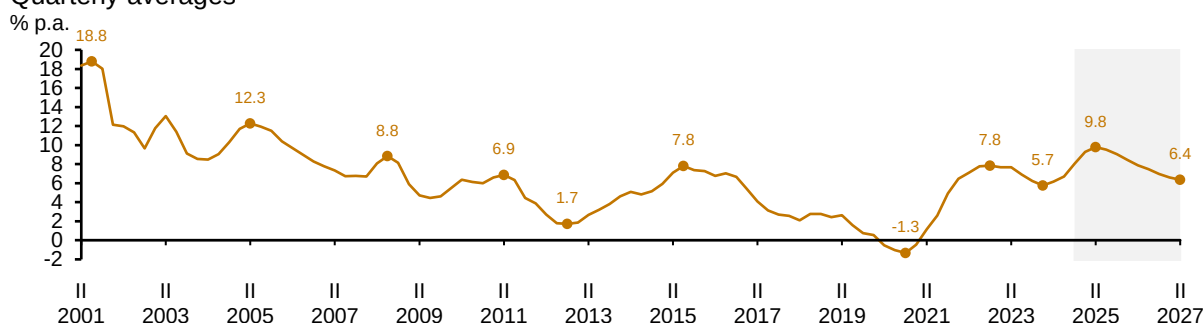
Copom considered that the magnitude of the short- and medium-term deterioration in the inflation scenario required a more timely policy action to maintain the firm commitment to converging inflation to the target. In its analysis, the Committee highlighted that the set of indicators on economic activity and labor market continues to exhibit strength, as observed in the release of GDP for 2024Q3, which suggests a further widening of the output gap. Headline inflation and measures of underlying inflation are above the inflation target and have increased in recent releases.

21. **Copom also stressed that, in light of a more adverse scenario for inflation convergence, the Committee anticipates, if the expected scenario confirms, adjustments of the same magnitude in the next two meetings.** Several risks have materialized, making the scenario more adverse but less uncertain, allowing the Committee to have greater visibility and then to provide an indication of how it anticipated the next decisions. The total magnitude of the tightening cycle will be determined by the firm commitment of reaching the inflation target and will depend on the inflation dynamics, especially the components that are more sensitive to economic activity and monetary policy, on the inflation projections, on the inflation expectations, on the output gap, and on the balance of risks.

22. **The rise in the Selic rate target and agents' expectations about its future movements led to a significant increase in the *ex-ante* real interest rate.** Considering the median expectations for the four-quarter-ahead Selic rate, discounted from inflation expectations, both taken from the Focus survey and measured in terms of quarterly averages, the *ex-ante* real interest rate, after reaching a local trough of 5.7% in 2024Q1, grows throughout the year, reaching 7.9% in 2024Q4 (Figure 14). Considering the implicit estimate in the Focus survey of January 3, 2025, the *ex-ante* real interest rate reaches a peak of 9.8% in 2025Q2, and then enters a downward trajectory, reaching 6.4% at the end of the considered horizon (2027Q2).

Figure 14 – Four-quarter-ahead real Selic rate

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. The values for 2025Q1-2027Q2 were calculated using data collected on 1/3/2025.

Source: BCB

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



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III - The expected time span for the measures to take effect

23. According to the projections of the reference scenario in the December IR⁷, inflation will remain above the limit of the tolerance interval until 2025Q3, after which it will enter a downward trajectory, but still remaining above the target. In this scenario, which uses the Selic rate from the Focus survey and the exchange rate following the PPP, inflation projections are above the upper limit of the tolerance interval of 4.50%, referring to the target of 3.00%, until 2025Q3 (Table 3 and Figure 15). Still in this scenario presented in the December IR, the projections for four-quarter inflation are 4.5% for 2025 (value, therefore, equal to the upper limit of the tolerance interval), 4.2% for 2026Q1 (therefore, lower than the upper limit), 4.0% for the relevant monetary policy horizon, considered in December to be 2026Q2, and 3.6% for 2026. As previously highlighted, inflation expectations from the Focus survey have increased more strongly in recent months, with the median of the January 3, 2025 survey standing at 5.0% for 2025, 4.0% for 2026, and 3.9% for 2027 (Figure 16)."

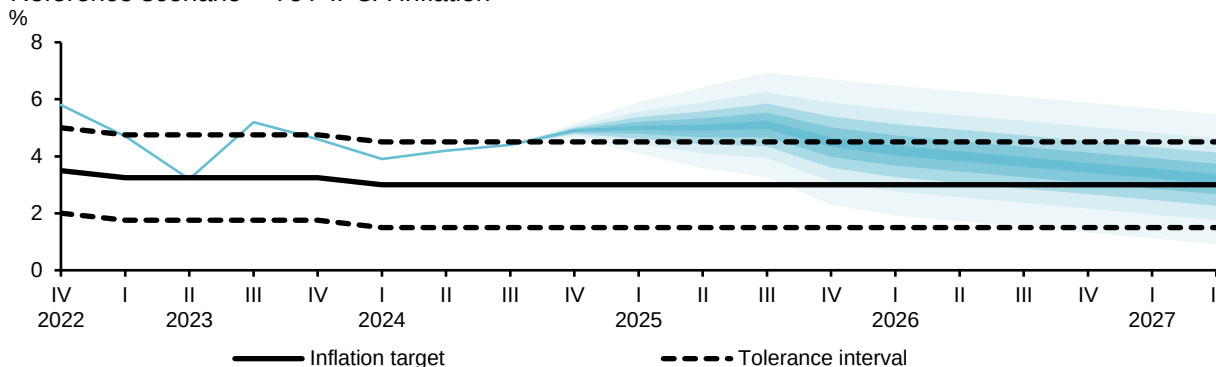
Table 3 – Inflation projections in the December 2024 Inflation Report – Reference scenario
YoY IPCA inflation

Price index	2023				2024					2025				2026				2027		%
	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	
IPCA	4.6	3.9	4.2	4.4	4.9	5.0	5.0	5.1	4.5	4.2	4.0	3.8	3.6	3.4	3.2					

Note: White background for actual values; hatched background for projections.

Figure 15 – Inflation projections and fan chart in the December 2024 Inflation Report

Reference scenario – YoY IPCA inflation



Note: The shaded areas represent projections intervals associated with the following probabilities (from the inner to the outer interval): 10%, 30%, 50%, 70% and 90%. Until 2024Q4, inflation targets and tolerance ranges refer only to the respective calendar year but, for visual reasons, the respective lines are presented for all quarters.

Source: BCB

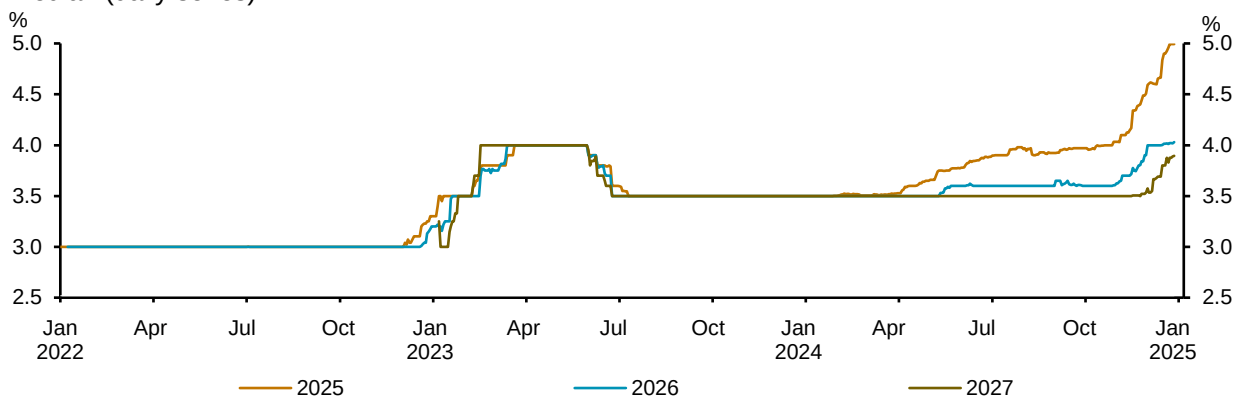
⁷ Elaborated with information available until December 11, 2024, using the trajectory for the interest rate extracted from the Focus survey of December 6, 2024 and the exchange rate starting from USD/BRL 5.95 (rounded average of the average exchange rate observed over the ten working days ending on the last day of the week prior to the Copom meeting) and evolving according to the purchasing power parity (PPP).

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br

Figure 16 – Focus survey inflation expectations for 2025-2027

Median (daily series)



Note: The figure data range is 1/4/2022 – 1/3/2025
Source: BCB

24. **At its most recent meeting (267th meeting), Copom highlighted that, due to the materialization of risks, it judges that the scenario is less uncertain and more adverse than at the previous meeting and that, nevertheless, the risks to its inflation scenarios remain tilted to the upside.** Among the upside risks for the inflation outlook and inflation expectations, it should be emphasized (i) a more prolonged period of deanchoring of inflation expectations; (ii) a stronger-than-expected resilience of services inflation due to a more positive output gap; and (iii) a conjunction of internal and external economic policies with an inflationary impact, for example, through a persistently more depreciated currency. Among the downside risks, it should be noted (i) a greater-than-projected deceleration of global economic activity; and (ii) an impact on global inflation larger than expected from monetary policy tightening.

25. **At the same meeting, Copom announced:**

The current scenario is marked by additional deanchoring of inflation expectations, an increase of inflation projections, a stronger-than-expected economic activity, and further widening of the output gap, which requires an even more contractionary monetary policy.

Copom therefore decided to increase the Selic rate by 1.00 p.p. to 12.25% p.a., and judges that this decision is consistent with the strategy for inflation convergence to a level around its target throughout the relevant horizon for monetary policy. Without compromising its fundamental objective of ensuring price stability, this decision also implies smoothing economic fluctuations and fostering full employment.

In light of a more adverse scenario for inflation convergence, the Committee anticipates further adjustments of the same magnitude in the next two meetings, if the scenario evolves as expected. The total magnitude of the tightening cycle will be determined by the firm commitment of reaching the inflation target and will depend on the inflation dynamics, especially the components that are more sensitive to

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br



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economic activity and monetary policy, on the inflation projections, on the inflation expectations, on the output gap, and on the balance of risks.

26. Therefore, the BCB has adopted appropriate measures for inflation to reach the target established by the CMN Resolution 5,141 of June 26, 2024, of 3.00%, effective as of January 2025, within the inflation-targeting framework established by Decree 12,079 of 2024.

Sincerely,

Gabriel Muricca Galípolo
Governor

Verified by

Cristiano Cozer
General Counsel of the Banco Central do Brasil
Registers: OAB/DF 16.400 – BCB 2.191.156-8

Governor

SBS Quadra 3, Bloco B, Edifício Sede – 20º andar
70074-900 – Brasília (DF)
Telephone: (61) 3414-1000
E-mail: presidencia@bcb.gov.br