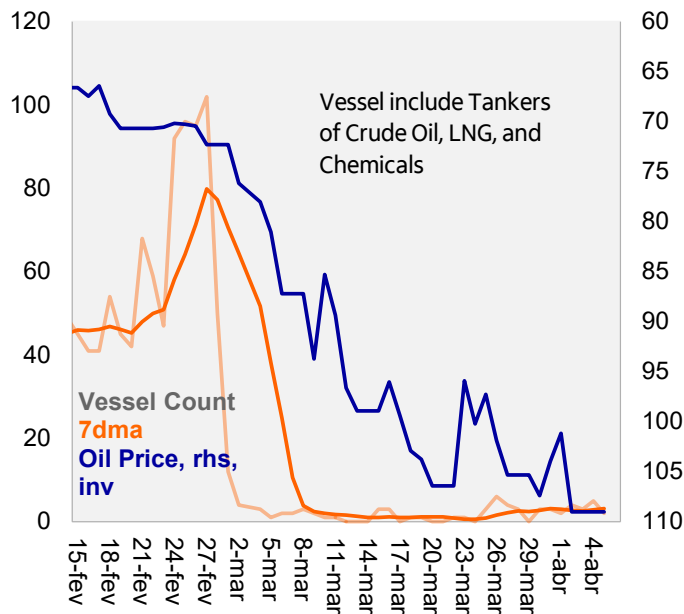


Oil shock and central bank reaction

- ▶ The blockade of the Strait of Hormuz, a corridor responsible for around 20% of global oil consumption, has triggered the largest supply disruption in history, with Brent prices jumping above USD 100/bbl. Despite the existence of buffers—such as some rerouting of regional production through alternative channels—if normalization does not occur, we estimate that the commodity could reach up to USD 180/bbl within three months.
- ▶ For central banks, the scenario brings significant uncertainty. In theory, a monetary authority should focus on the second-round effects of a supply shock, such as the spillover of inflation into more inertial items and into longer-term expectations. However, historically, oil shocks have been persistent and have therefore led to monetary tightening. In addition, the recent experience of 2022 should serve as a lesson and reinforce the need for a more cautious response by central banks.
- ▶ In some advanced economies, such as the United States and the United Kingdom, where inflation starting point is higher, the current shock is already sufficient to rule out interest rate cuts this year. If the rise in oil prices is not reversed in the short term, rate hikes become more likely at the ECB and the BoE, which have signaled that even if oil remains only temporarily above USD 100/bbl, they could raise rates starting in June. The Fed, on the other hand, given its dual mandate of activity and inflation, would likely wait longer and only raise rates if the increase in oil prices were seen as more persistent.
- ▶ For Brazil, synchronization with other central banks is not mechanical, but supply shocks tend to be amplified in an environment of unanchored expectations and resilient activity. As a result, the size of the monetary easing cycle initiated at the last Copom meeting now appears more limited than before the shock.

The war in Iran and the blockade of the Strait of Hormuz represent the largest disruption ever recorded in the global oil market, pushing prices to between USD 100/bbl and USD 120/bbl in recent weeks. Flows through the Strait account for around 20% of global oil consumption and have been virtually halted since the beginning of the conflict on February 27 (see chart). For comparison, the largest previous shocks resulted in disruptions of around 8% of oil production at the time. It is worth noting, however, that global GDP was significantly more oil-intensive during past oil shocks than it is today.

Daily vessel count through the Strait of Hormuz and oil prices

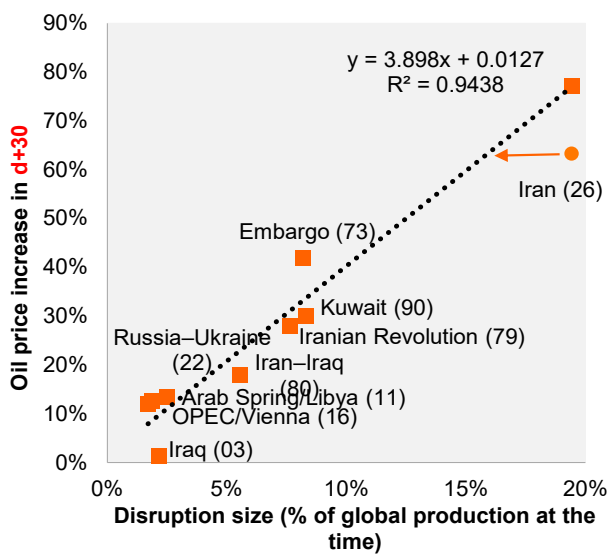


Source: Bloomberg, Itaú

On the one hand, oil prices during the first 30 days of the conflict (see 1st chart) appeared to price in a supply disruption somewhere between the maximum possible scenario (around 20% of global production) and a scenario that accounts for mitigating factors (around 10%). Advanced economies announced the release of 300–400 million barrels from strategic reserves. In addition, Middle Eastern countries have the capacity to reroute part of their production through the Red Sea, and there are also oil barrels already in transit.

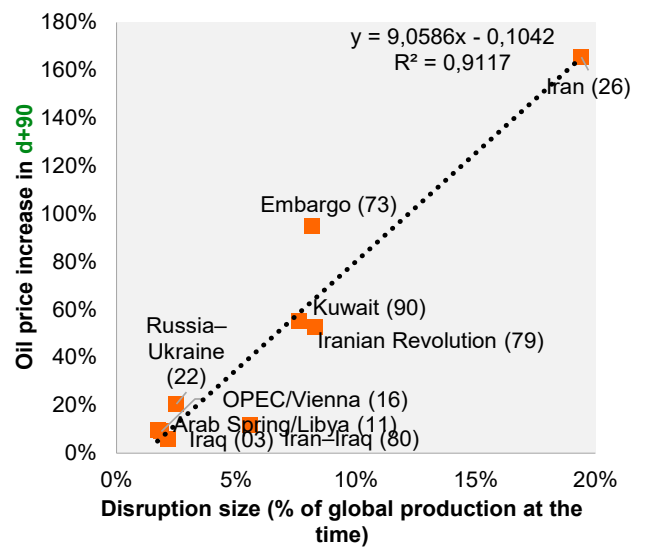
On the other hand, if the war or its effects on oil supply prove to be more prolonged, prices are expected to rise progressively over time. Historical correlations indicate that there is a risk of oil prices reaching USD 180/bbl if no normalization occurs within three months, representing a 160% increase relative to the beginning of the conflict.

Oil market disruption and prices after 30 days



Source: Bloomberg, Itaú

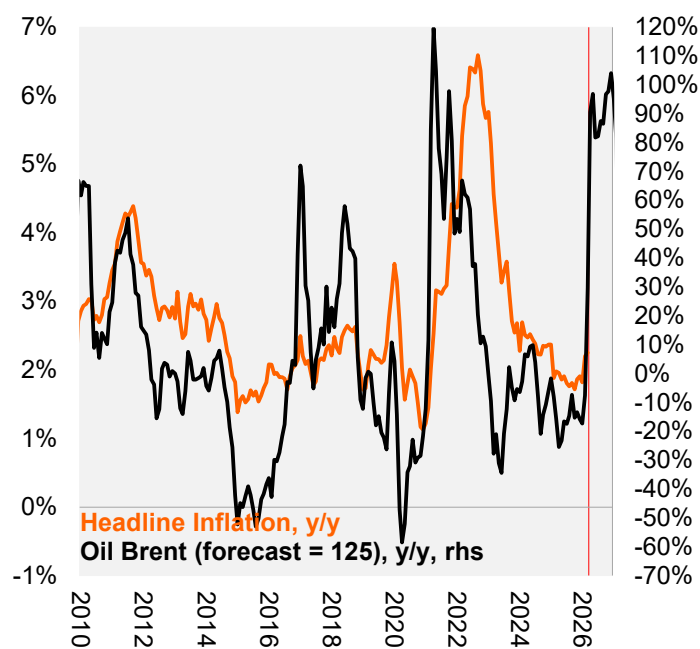
Oil market disruption and prices after 90 days



Source: Bloomberg, Itaú

For central banks, the environment has been volatile and marked by significant uncertainty. At current oil price levels, global inflation could rise to around 5% (see chart).

Global inflation may remain above 5%

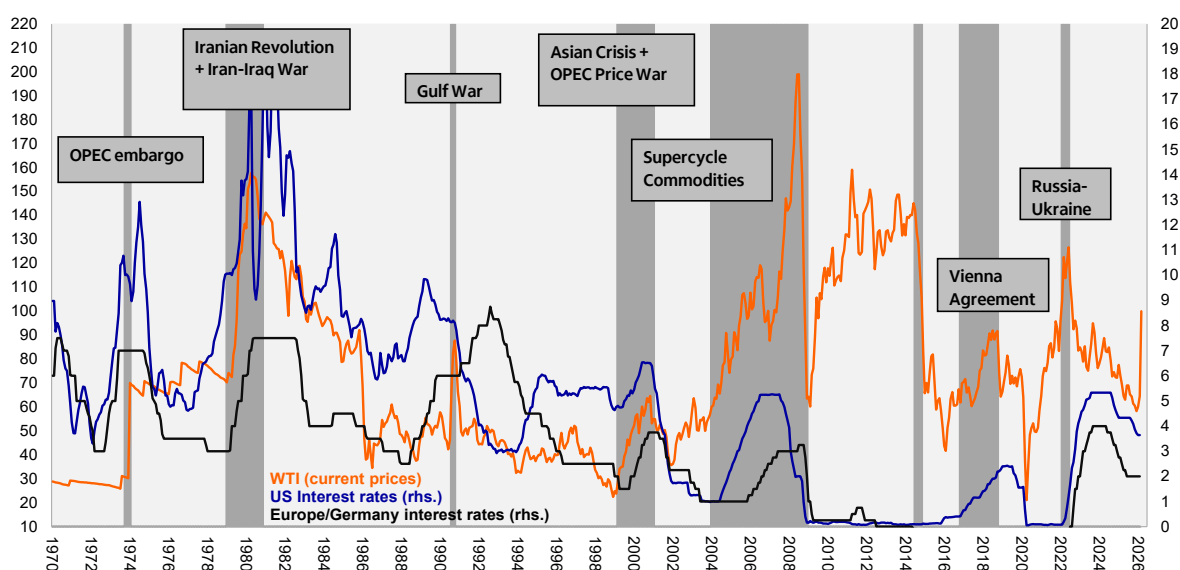


Source: Bloomberg, Itaú

In theory, a monetary authority should not react to a supply shock that has only a temporary impact on inflation and should instead focus on combating second-round effects. The objective should be to prevent the shock from propagating persistently, for instance through indexation mechanisms and pass-through into other components of current inflation and expectations. Within this framework, central banks may limit themselves to monitoring the primary shock, but they should react to signs that inflation will not be transitory and could threaten the inflation target beyond the short term.

However, historically, oil shocks have usually been persistent and have led to monetary tightening by central banks (see chart). Episodes such as the OPEC embargo (1973), the Iranian Revolution (1979) followed by the Iran–Iraq War, the Asian crisis combined with OPEC’s price war (1999), the commodity supercycle that extended through much of the first decade of the 2000s, the Vienna Agreement (2016), and the post-Covid supply constraint shock in 2021 followed by Russia’s invasion of Ukraine in 2022, were accompanied by interest rate hiking cycles by the Fed and the ECB, as well as other central banks around the world. The exception was the Gulf War episode (1990), in which the increase in oil prices was quickly reversed due to the short duration of the conflict.

Oil shocks and central bank reactions

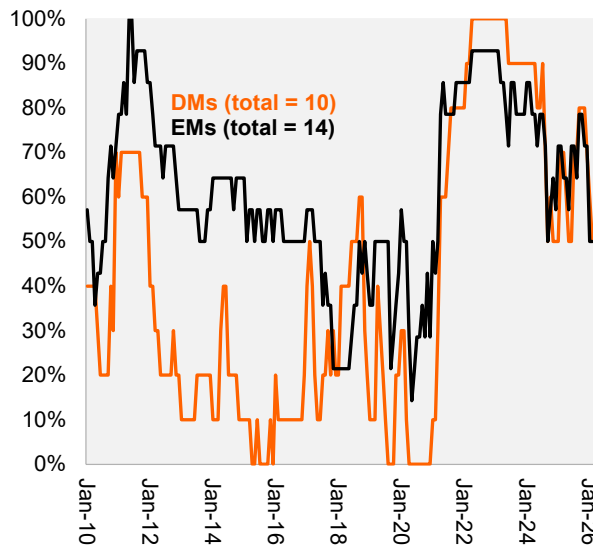


Source: Haver, Itaú

In addition, the 2021–22 experience should serve as a lesson and call for additional caution against once again merely monitoring the shock patiently. At the time, in the face of both supply and demand shocks, central banks placed greater weight on downside risks to economic activity and chose to treat inflationary pressures as transitory. This resulted in a degree of initial leniency toward inflation, which subsequently had to be corrected through a more forceful monetary tightening. A global environment of strong support for economic activity, driven by expansionary fiscal and monetary policies in the aftermath of the pandemic, laid the groundwork for the inflationary shock of 2021, which was further exacerbated by the energy shock following Russia’s invasion of Ukraine the following year. Central banks treated inflation as transitory and, months later, proved to be mistaken, being forced to raise interest rates more rapidly and to keep them higher for longer than initially expected.

Although the current scenario differs from that of 2022, many countries still exhibit inflation above target, inflation expectations remain above pre-pandemic levels, and the fundamentals supporting economic activity—such as expansionary fiscal policy and accommodative financial conditions, remain strong. In particular, the share of advanced economies with inflation above target has converged to that of emerging markets, which have historically been more prone to inflationary problems (see chart).

High share of central banks with inflation above target

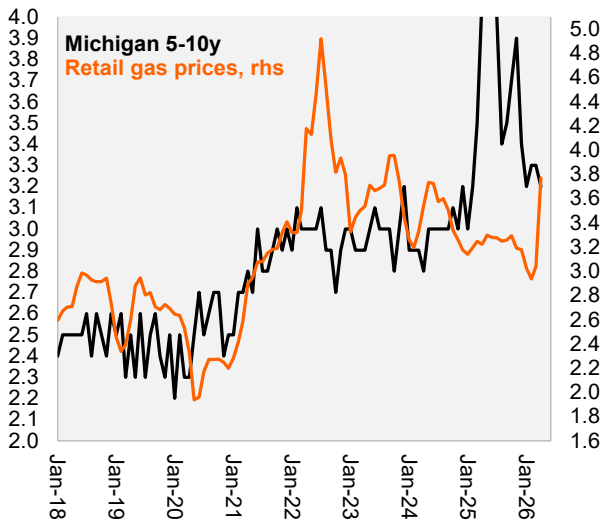


Source: Haver, Itaú

In the current shock, the initial reaction of advanced economy central banks has generally been to highlight the increase in inflationary risks (see summary table in the appendix). None of these central banks has cut interest rates, in contrast to expectations immediately prior to the conflict in the Middle East. The Fed, BoC, Riksbank, ECB, and BoE kept policy rates unchanged and conveyed a message of heightened caution, while the BoJ and the RBA signaled a higher likelihood of further rate hikes.

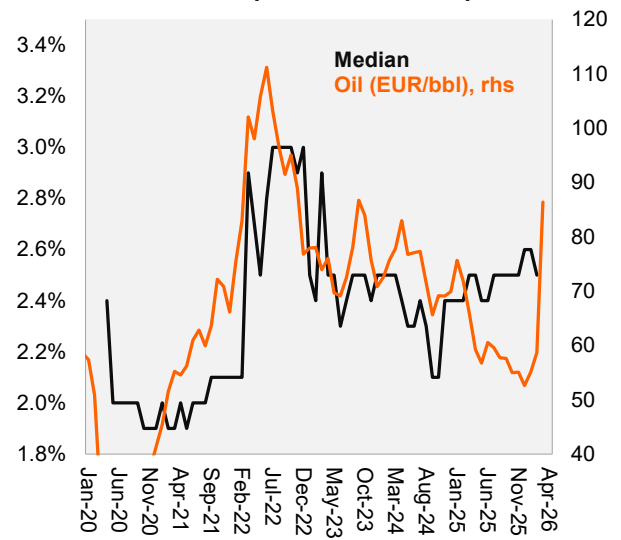
All central banks emphasized the risk to inflation expectations, which could rise and potentially become unanchored if oil prices remain elevated for a prolonged period (see charts for the United States and the Euro Area below).

US: inflation expectations and gasoline prices



Source: Haver, Itaú

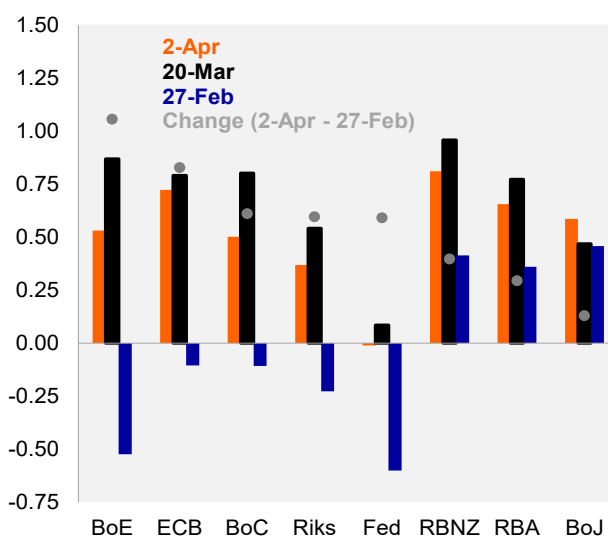
Euro Zone: inflation expectations and oil prices



Source: Haver, Itaú

Market pricing moved significantly, coming to embed at least one interest rate hike this year for all central banks, with the exception of the Fed.

Pricing of interest rate changes in 2026: today versus pre-shock



Source: Bloomberg, Itaú

To assess whether this expected central bank reaction will materialize, it is important to consider the starting point in terms of macroeconomic conditions. Past cycles began from less favorable initial conditions, either with very high inflation, as in the 1970s and 1980s, or with policy rates low relative to the neutral level, as in the 2000s. In episodes where inflation is already elevated, an additional shock is particularly concerning, as there is little buffer to absorb higher energy costs. In scenarios where interest rates are considered expansionary, the shock calls for a swift monetary policy response.

Condições da economia pré-choque										
Evento	OPEC embargo (73)	Iranian Revolution (79) + Iran-Iraq War	Gulf War (90)	Asian Crisis + OPEC price war (99)	Commodities supercycle (04)	Shale + OPEC no-cut decision (14)	Shale rebound + OPEC Vienna agreement (16)	Supply constraints (21) + Ukraine war (22)	Iran (26)	
Month	Oct-73	Jan-79	Aug-90	Jan-99	Jan-04	Jun-14	Nov-16	Feb-22	Feb-26	
Oil disruption (mbd)	8%	8%	8%	-	-	-	-	3%	19%	
Brent (current prices)	20	58	35	21	47	144	62	86	62	
United States										
Headline PCE	6.1%	7.5%	3.9%	0.8%	2.1%	1.8%	1.4%	6.3%	2.8%	
Core PCE	4.3%	6.9%	4.1%	1.4%	1.6%	1.6%	1.8%	5.4%	3.1%	
Long-term expectations	-	-	4.2%	2.9%	2.8%	2.8%	2.4%	3.1%	3.3%	
Fed policy rate	10.8%	10.0%	8.0%	4.8%	1.0%	0.1%	0.4%	0.1%	3.6%	
Policy rate minus neutral	4.8%	4.3%	2.5%	-0.7%	-3.8%	-2.8%	-2.6%	-3.4%	0.5%	
Unemployment rate	4.8%	6.0%	5.5%	4.4%	5.7%	6.3%	4.9%	4.0%	4.3%	
Minus NAIRU	-1.3%	-0.2%	-0.2%	-0.8%	0.7%	1.5%	0.3%	-0.4%	-0.1%	
Payrolls, last 12 months	3012	4261	1746	3046	124	2417	2486	7143	290	
Euro area										
Headline CPI	-	-	-	-	2.1%	0.5%	0.5%	5.1%	1.9%	
Core CPI	-	-	-	-	1.6%	0.7%	0.7%	2.3%	2.4%	
Long-term expectations	-	-	-	-	1.9%	1.8%	1.8%	2.0%	2.0%	
ECB policy rate	7.00%	3.00%	6.00%	2.50%	1.00%	0.00%	-0.40%	-0.50%	2.00%	
Policy rate minus neutral	1.8%	-1.5%	1.5%	-1.4%	-3.2%	-2.2%	-2.9%	-3.1%	0.0%	
Unemployment rate	-	-	-	-	9.4%	11.8%	9.8%	6.9%	6.1%	
United Kingdom										
Headline CPI	-	-	6.7%	1.6%	1.3%	1.5%	0.9%	5.4%	3.0%	
Core CPI	-	-	6.7%	1.5%	1.1%	1.6%	1.0%	4.3%	3.2%	
Long-term expectations	-	-	-	-	-	2.9%	3.1%	3.3%	3.7%	
BoE policy rate	11.50%	12.50%	14.88%	6.25%	3.75%	0.50%	0.25%	0.25%	3.75%	
Policy rate minus neutral	6.0%	7.8%	10.1%	2.1%	-0.6%	-3.1%	-3.4%	-3.3%	0.2%	
Unemployment rate	3.5%	5.3%	7.0%	6.2%	4.8%	6.3%	4.8%	3.9%	5.2%	

*Euro area rates: Germany up to 2000, ECB after 2000
Source: Haver, Itaú

In the United States, inflation remains above target, with interest rates close to the neutral level. Economic activity continues to be resilient, supported by expansionary fiscal policy, still-solid household balance sheets, favorable financial conditions even after the recent tightening, and strong infrastructure investment linked to AI, which has been boosting productivity. Although employment growth has slowed to close to zero, this backdrop of solid activity is likely to stabilize unemployment without a rise in layoffs. On the other hand, inflation shows signs of persistence above target. Despite being lower than in 2022, the initial conditions under which the current supply shock is occurring are unfavorable, and core inflation is likely to move toward a seventh consecutive year above target (2021–27), increasing the risk of spillovers into inflation expectations.

This has led the Fed to adopt a more cautious stance regarding interest rate cuts and could even result in a new tightening cycle if the shock intensifies. Using the Fed’s own model estimates for the impact of oil on inflation and activity—where a 10% increase in oil prices leads to a 5 basis point increase in core inflation and a 5 basis point reduction in activity—together with Taylor rule specifications described in Fed documents, we present scenario simulations for the oil shock in the table below. Assuming Brent oil prices remain permanently at USD 100/bbl (orange box) or USD 130/bbl (red box), Core PCE inflation rises above 3.0% and, despite generating increases in unemployment, indicates the need for more than one interest rate hike to meet the 2.0% inflation target, should that indeed remain the ultimate policy objective.

USA: Average of Taylor Rules* (assumptions: r-star = 1.0%; Nairu 4.2%)							
Core PCE	Unemployment						
	4.2	4.3	4.4	4.5	4.6	4.7	4.8
2.2	3.4	3.2	3.1	3.0	2.8	2.7	2.6
2.3	3.5	3.4	3.2	3.1	3.0	2.8	2.7
2.4	3.6	3.5	3.3	3.2	3.1	2.9	2.8
2.5	3.7	3.6	3.4	3.3	3.2	3.0	2.9
2.6	3.8	3.7	3.6	3.4	3.3	3.2	3.0
2.7	3.9	3.8	3.7	3.5	3.4	3.3	3.1
2.8	4.1	3.9	3.8	3.6	3.5	3.4	3.2
2.9	4.2	4.0	3.9	3.8	3.6	3.5	3.4
3.0	4.3	4.1	4.0	3.9	3.7	3.6	3.5
3.1	4.4	4.3	4.1	4.0	3.8	3.7	3.6
3.2	4.5	4.4	4.2	4.1	4.0	3.8	3.7
3.3	4.6	4.5	4.3	4.2	4.1	3.9	3.8
3.4	4.7	4.6	4.5	4.3	4.2	4.0	3.9
3.5	4.8	4.7	4.6	4.4	4.3	4.2	4.0
3.6	5.0	4.8	4.7	4.5	4.4	4.3	4.1
3.7	5.1	4.9	4.8	4.7	4.5	4.4	4.2

Green = March meeting projection, which incorporated part of the shock; Orange = oil at USD 100/bbl; Red = oil at USD 130/bbl.

*Avg of Taylor (1993), Inertial (1993), Balanced-approach (shortfalls) and First-difference rules

Source: Itaú

In the case of the ECB, the scenario is more benign, with inflation close to target, moderate economic activity, and interest rates around the neutral level. However, given the continent’s high exposure to oil and gas prices and the monetary authority’s mandate, which is exclusively focused on inflation control, a tightening cycle would likely come sooner than in the case of the Fed if the conflict were to persist. At its March monetary policy meeting, the ECB presented three energy price scenarios: a baseline scenario, with oil and gas prices rising to USD 90/bbl and EUR 50/MWh and then returning to USD 60/bbl and EUR 30/MWh, respectively; an alternative scenario, with a sharper increase to USD 120/bbl and EUR 90/MWh, but still converging back to the same final levels as in the baseline; and, finally, a severe scenario, in which oil prices rise to USD 120/bbl and remain close to USD 100/bbl in the following years, while gas prices increase to EUR 105/MWh and later decline to EUR 40/MWh. We estimate several Taylor rules, that is, monetary policy reaction functions, for these scenarios. The estimates show that, should the baseline scenario materialize, policy rates at 2% would still be warranted. However, at least two to four rate hikes would be prescribed under the (plausible) adverse and severe scenarios, respectively.

EZ: Average of Taylor Rules* (assumptions: r-star = 0%, NAIRU = 6.3%)											
Core HICP	Unemployment										
	6.0	6.1	6.2	6.3	6.4	6.5	6.6	6.7	6.8	6.9	7.0
2.0	2.5	2.3	2.2	2.0	1.9	1.8	1.7	1.6	1.5	1.4	1.3
2.1	2.6	2.4	2.3	2.1	2.0	1.9	1.8	1.7	1.6	1.5	1.4
2.2	2.7	2.5	2.4	2.2	2.1	2.0	1.9	1.8	1.7	1.6	1.5
2.3	2.8	2.6	2.5	2.4	2.3	2.2	2.1	2.0	1.9	1.8	1.7
2.4	2.9	2.7	2.6	2.5	2.4	2.3	2.2	2.1	2.0	1.9	1.8
2.5	3.0	2.9	2.7	2.6	2.5	2.4	2.3	2.2	2.1	2.0	1.9
2.6	3.1	3.0	2.8	2.7	2.6	2.5	2.4	2.3	2.2	2.1	2.0
2.7	3.2	3.1	2.9	2.8	2.7	2.6	2.5	2.4	2.3	2.2	2.1
2.8	3.3	3.2	3.0	2.9	2.8	2.7	2.6	2.5	2.4	2.3	2.2
2.9	3.4	3.3	3.1	3.0	2.9	2.8	2.7	2.6	2.5	2.4	2.3
3.0	3.5	3.4	3.3	3.1	3.0	2.9	2.8	2.7	2.6	2.5	2.4
3.1	3.6	3.5	3.4	3.2	3.1	3.0	2.9	2.8	2.7	2.6	2.5
3.2	3.7	3.6	3.5	3.3	3.2	3.1	3.0	2.9	2.8	2.7	2.6
3.3	3.9	3.7	3.6	3.4	3.3	3.2	3.1	3.0	2.9	2.8	2.7
3.4	4.0	3.8	3.7	3.5	3.4	3.3	3.2	3.1	3.0	2.9	2.8
3.5	4.1	3.9	3.8	3.7	3.6	3.5	3.4	3.3	3.2	3.1	3.0
3.6	4.2	4.0	3.9	3.8	3.7	3.6	3.5	3.4	3.3	3.2	3.1
3.7	4.3	4.1	4.0	3.9	3.8	3.7	3.6	3.5	3.4	3.3	3.2
3.8	4.4	4.3	4.1	4.0	3.9	3.8	3.7	3.6	3.5	3.4	3.3
3.9	4.5	4.4	4.2	4.1	4.0	3.9	3.8	3.7	3.6	3.5	3.4
4.0	4.3	4.2	4.1	4.0	3.8	3.7	3.6	3.5	3.3	3.2	3.1

*Avg Taylor (1993), Balanced=approaches with shortfalls; First-time difference and ECB rule.

Scenarios: green = before the conflict; blue = baseline after the conflict; yellow = adverse and red = severe.

Source: Itaú

The BoE, in turn, faces a situation more similar to that of the United States, with core inflation above target and interest rates slightly above neutral (currently at 3.75%). Despite core inflation remaining under pressure, until shortly before the shock the expectation was that headline inflation would converge to 2.0% as early as next quarter, driven by lower energy costs (green box in the table below). Based on the BoE's estimates and Taylor rules, with oil prices at USD 100/bbl (orange box), a 25 bp rate hike would be justified, although the central bank would likely avoid such a move if the shock were perceived as transitory. With oil at USD 130/bbl (red box), however, inflation exceeds 5.0% and, even with rising unemployment, the rule suggests more than one rate increase to bring inflation back to the 2.0% target.

UK Average of Taylor Rules* (assumptions; R-star = 3.5%; Nairu = 5%)										
CPI	UR									
	4.0%	4.5%	5.0%	5.3%	5.5%	5.8%	6.0%	6.5%	7.0%	
1.8%	4.2	4.0	3.8	3.6	3.5	3.4	3.3	3.1	2.9	
2.0%	4.4	4.0	3.8	3.7	3.6	3.5	3.4	3.1	2.9	
2.5%	4.6	4.2	4.0	3.8	3.7	3.6	3.5	3.3	3.1	
3.0%	4.8	4.3	4.1	4.0	3.9	3.8	3.7	3.4	3.2	
3.5%	5.0	4.5	4.3	4.1	4.0	3.9	3.8	3.6	3.4	
4.0%	5.2	4.6	4.4	4.3	4.2	4.0	4.0	3.7	3.5	
4.5%	5.4	4.8	4.6	4.4	4.3	4.2	4.1	3.9	3.7	
5.0%	5.6	4.9	4.7	4.6	4.5	4.3	4.2	4.0	3.8	
5.5%	5.8	5.1	4.8	4.7	4.6	4.5	4.4	4.2	3.9	
6.0%	6.0	5.2	5.0	4.9	4.8	4.6	4.5	4.3	4.1	

Green = BoE scenario before the shock; Orange = oil at USD 100/bbl; Red = oil at USD 130/bbl.

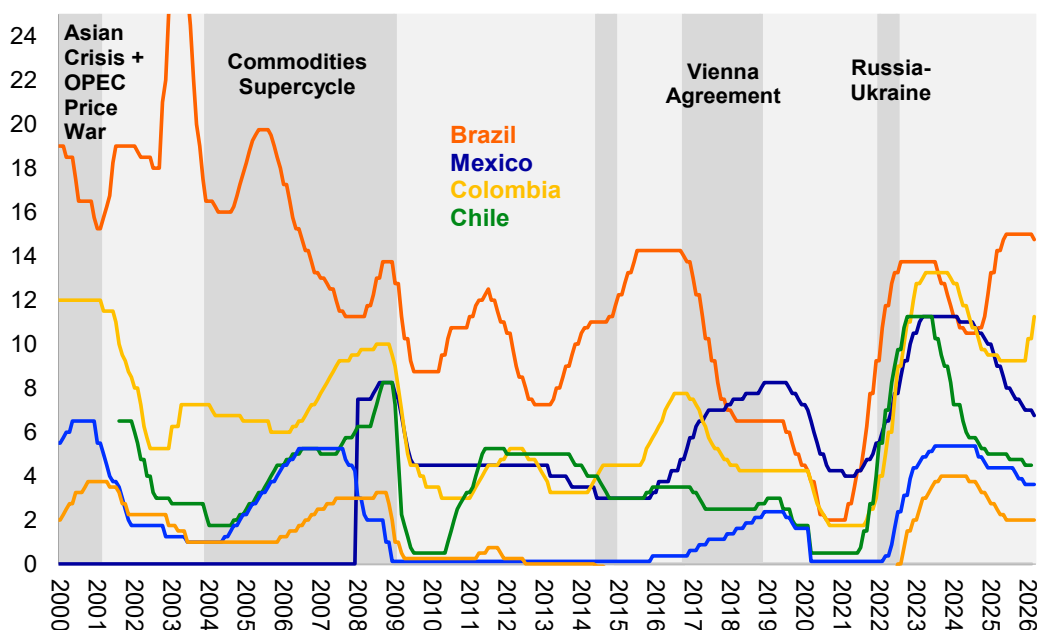
*Average of BoE contemporaneous, BoE first difference and classic first-difference rules

Source: Itaú

For Brazil, the synchronization of monetary policy with other central banks during supply shocks is less direct and conditional on domestic factors, such as exchange rate dynamics, the output gap, and the degree

of anchoring of inflation expectations. During the commodity supercycle, the strong appreciation of the Brazilian real acted as a disinflationary force, while under the Vienna Agreement the rise in oil prices coincided with a post-recession disinflationary environment and well-anchored expectations, reducing the need for a monetary response aligned with that of other central banks. By contrast, during the Russia–Ukraine conflict, the Central Bank of Brazil (BCB) was already in a tightening cycle and ultimately was unable to interrupt it in the face of the additional shock, indicating that in an environment of elevated inflation and unanchored expectations, supply shocks tend to be amplified.

Monetary policy synchronization is limited – Brazil vs. other countries



Source: Haver, Itaú

In light of the oil shock and the deterioration of the inflationary outlook, with inflation expectations rising even at longer horizons, the room for continuing the monetary easing cycle initiated at the last meeting has become more limited, although it is not zero. Simulations from the Central Bank’s inflation model indicate that, if the oil price curve remains at current levels and there is no further deterioration in expectations, there is still room for a small interest rate cut cycle (of approximately 1 percentage point), smaller than the 2.5 percentage points expected prior to the shock.

		Inflation in relevant horizon (Q4 2027) with Selic rate unchanged at 14.75%		Selic rate needed to bring inflation down to 3.3%.	
Oil →		Pre-war curve	Curve today	Pre-war curve	Curve today
Focus 26/27/28	Pre war: 3.9 / 3.8 / 3.5	2.5	2.8	12.25	13.25
	Focus today (5d): 4.5 / 3.9 / 3.7	2.6	3.0	12.75	13.75

BRL 5.15 in all simulation

Source: Itaú

In summary, historical context and recent experience suggest that the inflationary risks stemming from a new oil shock may be significant, and that central banks should monitor this risk carefully and, in contrast to 2022, react swiftly to prevent further de-anchoring of inflation expectations.

Appendix: Summary of monetary policy meetings of advanced economy central banks following the onset of the conflict in Iran.

Central Bank	Bottom line message	Policy Decision	Communication response to the War/Oil shock				Itaú Scenario (current vs prior)
			Statement	Press Conference	Scenario/Forecasts		
					Inflation	GDP	
Fed	cautious on cuts	hold (7-2)	implications are uncertain.	higher energy prices will push up inflation, but too soon to know scope and duration of effects... No inflation progress would mean no cuts	26 +30bps 27 +10bps	26 +10bps 27 +30bps	no cuts (vs 2)
BoC	cautious on cuts	hold	The breadth and duration of the conflict, and hence its economic impacts, are highly uncertain; We are also monitoring the unfolding conflict closely and assessing its impact on growth and inflation; we stand ready to respond as needed	GC will look through the war's immediate impact on inflation but if energy prices stay high, we will not let their effects broaden and become persistent inflation.	-	-	no cuts
Riksbank	reinforce a longer hold	hold (5-0)	expected to dampen growth somewhat in the near term and push up inflation, still too early to be able to see clearly how the war is affecting the outlook	-	26 +60bps 27 -40bps	26 -40bps 27 +10bps	-
ECB	cautious on cuts, forecasts open the door to hikes	hold (unanimous)	outlook significantly more uncertain, creating upside risks for inflation and downside risks for economic growth. It will have a material impact on near-term inflation through higher energy prices. Its medium-term implications will depend both on the intensity and duration	It will depend on how long the situation in the Middle East persists, could lead to constraints on supply. We will be watching closely to see how much this reflects in the sentiment	26 +70bps 27 +20bps (alternative scenarios)	26 -30bps 27 -10bps (alternative scenarios)	no cuts
BoE	cautious on cuts and open the door to hikes	hold (9-0)	Conflict in the Middle East has caused a significant increase in global energy and other commodity prices; Committee will continue to monitor closely the situation in the Middle East and its impact on global energy supply and energy prices. It stands ready to act as necessary	Bailey: very different from 2022, cautious against "strong conclusions" on rate hikes	2Q26 +90bps 3Q26 +160bps	-	no cuts (vs 1)
Norges	further hikes	hold	The war in the Middle East has led to high volatility in energy and financial markets. Oil and gas prices have increased sharply. At the same time, global equity indices have declined, and interest rates have increased both abroad and in Norway. Higher energy prices will likely reduce global growth and push up inflation both abroad and in Norway.	Uncertainty is greater than normal due to the war in the Middle East, but the Committee judges that it will likely be necessary to raise the policy rate at one of the forthcoming monetary policy meetings	26 +100bps 27 -30bps	26 0bps 27 -20bps	-
RBA	further hikes	+25bps (5-4)	poses substantial risks in both directions; sharply higher fuel prices, which, if sustained, will add to inflation. Short-term measures of inflation expectations have already risen. As a result, the Board judged that there is a material risk that inflation will remain above target for longer than previously anticipated.	Higher petrol prices will add to inflation, not the reason for today's decision... If we do not act, these price pressures will spread and the eventual adjustment would be harder. This all suggests that the risks to inflation have tilted to the upside.	-	-	-
BoJ	further hikes	hold (8-1)	The rate of increase is then expected to come under upward pressure, affected by the recent rise in crude oil prices, Attention should also be paid to the impact	create inflationary pressure, downward pressure on activity...depend on war duration, will be watching closely	-	-	2 hikes

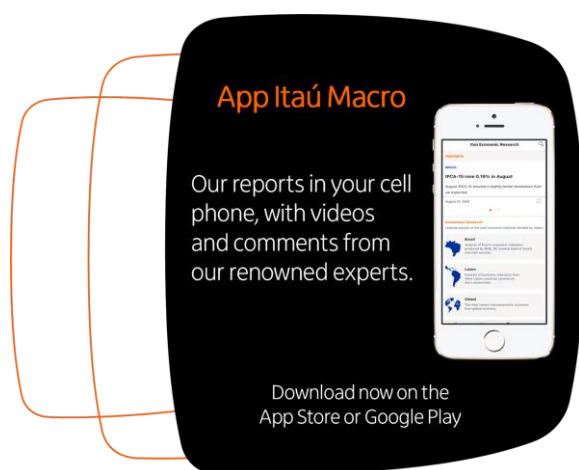
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