

Monetary Policy Report: preserving flexibility

- ▶ The June Monetary Policy Report (MPR) showed an inflation projection of 3.7% in 4Q27, the relevant horizon for the decision that reduced the Selic rate to 14.25%. The projection was revised up by +0.4 p.p. relative to the previous MPR — with widespread increases across all quarters through the end of the relevant horizon and stable estimates for 2028, slightly above target (3.1% in both 3Q28 and 4Q28, the latter published for the first time).
- ▶ The revision to the current relevant horizon reflects (i) the upside surprise in recent IPCA prints; (ii) a higher estimate for the output gap; (iii) increases in oil, fuels, and other commodity prices; and (iv) a deterioration in inflation expectations. Conversely, the higher path for the Selic rate implied by the Focus survey and the exchange rate appreciation helped mitigate this increase. Notably, the projection drops from 3.7% in 4Q27 to 3.2% in 1Q28 — supporting the Copom's signal for convergence to the target in the first quarter of 2028 (the next relevant horizon).
- ▶ The sharp decline in the projection between 4Q27 and 1Q28 is largely supported by the revision to the output gap. The BCB raised the current level of the gap (0.5% in 1Q26 and 0.4% in 2Q26) — consistent with stronger activity in 1Q26 and a robust labor market — but projects a narrowing to negative values over the coming quarters, reaching -0.5% in 4Q27, largely due to restrictive monetary conditions. As the neutral interest rate assumption was kept unchanged (at 5.00%), the projected closing of the gap over the horizon contributes to bringing inflation down toward the end of the window. Additionally, the scenario incorporates the assumption of a strong El Niño, whose impact on inflation is initially upward but turns downward after three quarters.
- ▶ In our assessment, the set of information reinforces the message that the calibration cycle is almost done and will remain data-dependent, while the projections and the scenario description in the report preserve flexibility without compromising inflation convergence at the new relevant horizon.
- ▶ As usual, the MPR included relevant analytical boxes on both cyclical and structural issues. Among them, we highlight two boxes related to the Middle East conflict: the first consolidates the perceptions of analysts (QPC) and firms (Firmus) regarding the shock, showing convergence around a predominantly inflationary impact with limited effects on activity projections (median of 1.0 p.p. for the 2026 IPCA and 0.0 p.p. for GDP), while the second discusses initial impacts on the trade balance, consistent with Brazil's net oil exporter position. The third box analyzes how adverse shocks can significantly alter the risk distributions for inflation and growth, concluding that such shocks increase the probability of higher inflation or weaker growth scenarios. Finally, it is worth noting the box on the revision to the 2026 GDP projection, which was raised from 1.6% to 2.0%, mainly reflecting the positive surprise in 1Q26 and improved prospects for agriculture and extractive industries, in a context where fiscal and credit stimulus continues to support domestic demand.

Central Bank forecasts

The table below shows the inflation estimates released for the reference scenario.

	Central Bank inflation (IPCA) forecasts											
	2026				2027				2028			
	I	II	III	IV	I	II	III	IV	I	II	III	IV
IPCA	4.1	4.8	4.8	5.2	4.6	4.0	4.1	3.7	3.2	3.2	3.1	3.1
Difference to previous MPR (pp)	0.5	1.1	1.0	1.3	1.0	0.6	0.8	0.4	0.0	0.0	0.0	-
Market-set prices	3.7	4.6	4.8	5.3	5.0	4.1	4.0	3.7	3.2	3.1	3.1	3.1
Difference to previous MPR (pp)	0.4	1.3	1.3	1.6	1.5	0.7	0.7	0.4	0.0	0.0	0.0	-
Regulated prices	5.5	5.3	4.9	4.7	3.7	3.6	4.1	3.9	3.5	3.4	3.4	3.3
Difference to previous MPR (pp)	1.0	0.4	0.0	0.4	-0.1	0.0	0.9	0.5	0.2	0.2	0.3	-

*Painted area = forecasts.

Source: Central Bank

Compared to the estimates presented in the March MPR, inflation projections were revised upward across all quarters up to the end of the current relevant horizon (4Q2027), while estimates for 2028 remained stable and slightly above the inflation target. For 4Q2028, published for the first time, the projection stood at 3.1%, in line with that for 3Q2028.

The increase relative to the previous MPR, of +0.4 p.p. at the current relevant horizon, reflects: (i) the upside surprise in recent IPCA prints; (ii) a higher estimate for the output gap; (iii) higher oil, fuel, and other commodity prices; and (iv) a deterioration in inflation expectations. Conversely, the higher Selic path implied by the Focus survey and the exchange rate appreciation helped mitigate this increase.

Regarding the trajectory of projections, the report highlights factors behind the upward revision, notably the incorporation of a strong El Niño in the baseline scenario. The impact of the climate phenomenon on inflation is initially upward but turns downward after three quarters. In particular, considering the expected normalization of the climate anomaly from early 2027, the effect on 12-month IPCA inflation at the relevant horizon is described as relatively modest compared to what is expected for end-2026 and the first three quarters of 2027. From 2028 onward, the normalization of relative food prices is expected to exert a meaningful disinflationary contribution to inflation over four quarters.

There was also a significant revision to the output gap, estimated at 0.5% and 0.4% in the first and second quarters of 2026, respectively. The BCB projects that the gap will gradually move into negative territory over the coming quarters, reaching -0.5% in 4Q2027, largely due to restrictive monetary conditions. As the neutral interest rate assumption was kept unchanged (at 5.00%), the projected closing of the gap over the horizon contributes to bringing inflation down.

Additionally, the report clarifies that the assumed oil price path starts at USD 100/barrel in 2Q2026, declines to USD 85 in 1Q2027, and then grows at 2% per year. From that point onward, the assumed price path is about 10% higher than in the previous MPR. The projection also incorporates a gradual normalization of refining margins (crack spreads) for petroleum derivatives.

In our assessment, this set of information reinforces the message that the calibration cycle is almost done and will remain data-dependent, while the projections and the scenario description preserve flexibility without compromising inflation convergence at the new relevant horizon.

Regarding the usual BCB forecast revisions, the improvement in GDP growth projections (to 2.0% from 1.6%) reflects improved estimates for the agricultural, industrial, and services sectors. Expected agricultural growth increased from 1.0% to 1.7%, mainly driven by updates to IBGE's crop forecasts, with notable upward revisions for soybean, corn, and coffee production. In industry, growth projections were revised from 1.2% to 2.3%, reflecting improved estimates for extractive industries and construction (incorporating stronger-than-expected performance in the first quarter), as well as manufacturing (due to more favorable early signals in 2Q26 and the implementation of recent stimulus measures, particularly credit measures related to the automotive sector). From a demand perspective, estimates for domestic demand improved, with upward revisions to household consumption (from 1.4% to 2.1%) and gross fixed

capital formation (GFCF, from 0.5% to 1.5%), both influenced by stronger-than-expected first-quarter results and the anticipated effects of fiscal and credit-related stimulus. Conversely, the text notes that expectations of a higher interest rate path tend to mitigate this impulse.

Gross domestic product forecasts (accumulated in the year)			
	Actual	Previous	Actual
	2025	2026	2026
GDP (current prices)	2.3%	1.6%	2.0%
Agriculture and livestock	11.7%	1.0%	1.7%
Industry	1.4%	1.2%	2.3%
Services	1.8%	1.7%	1.9%
Household consumption	1.3%	1.4%	2.1%
Government consumption	2.1%	2.0%	2.0%
Gross fixed capital formation	2.9%	0.5%	1.5%
Exports	6.2%	2.5%	3.0%
Imports	4.5%	1.0%	2.0%

Source: Central Bank.

The projected nominal growth of credit in the National Financial System (SFN) for 2026 was maintained at 9.0%, marking a deceleration for the second consecutive year, reflecting a recent slowdown in growth and consistency with more moderate activity and the effects of monetary policy. Growth in non-earmarked credit slowed, particularly for corporations, while the household segment outperformed expectations, supported by private payroll loans, vehicle financing, and revolving credit card balances. Meanwhile, earmarked credit remained more dynamic than projected, driven by rural credit and BNDES financing, offsetting the loss of momentum in programs such as PEAC-FGI. Revisions to projections also reflect some impact from recent programs that both expand credit (Move Brasil, Pronampe) and reduce the stock of debt (Desenrola).

Credit balance growth forecasts (12-month change)			
	Actual	Current	Previous
	2025	2026	2026
Total	10.3%	9.0%	9.0%
Non-earmarked	8.7%	8.1%	7.8%
Households	13.5%	9.5%	10.0%
Corporations	2.3%	6.0%	4.5%
Earmarked	12.6%	10.2%	10.7%
Households	9.6%	9.5%	9.5%
Corporations	18.6%	11.5%	13.0%
Total households	11.7%	9.5%	9.8%
Total corporations	8.2%	8.2%	7.8%

Source: Central Bank.

Finally, the projection for the current account deficit in 2026 was revised to US\$ 56 bn (2.1% of GDP, from US\$ 58 bn), indicating improvement relative to the previous report and the 2025 outcome, mainly driven by a stronger trade balance. The trade surplus was revised upward, supported by higher international prices (particularly oil, soybeans and beef) alongside higher imports largely due to fuel price effects.

External accounts forecasts (USD billion)			
	Actual	Current	Previous
	2025	2026	2026
Current account	-67	-58	-56
Trade balance	60	73	78
Exports	351	374	385
Imports	291	301	307
Services	-51	-54	-56
Primary income	-81	-82	-83
FDI	78	70	75

Source: Central Bank.

Summary of the studies

We present below summaries of the studies published in this edition.

Inflation and economic activity risk analysis

Full study in Portuguese [here](#).

- The study applies quantile regressions to estimate conditional distributions of inflation and growth, allowing the assessment of asymmetries and the distribution of risks around central trajectories, complementing traditional macroeconomic forecasting approaches.
- For inflation, the projected distribution shows positive skewness, with a median close to Focus expectations, but with a meaningful probability of exceeding the upper bound of the target; demand and cost shocks increase this risk by shifting the distribution to higher levels and raising concentration in the upper tail.
- For economic activity, the growth-at-risk approach indicates that financial conditions and the yield curve mainly affect the lower quantiles of growth, increasing the likelihood of low-growth or recession scenarios in response to adverse shocks.
- The results show that macroeconomic shocks affect not only central projections but also the dispersion and asymmetry of distributions, reinforcing the importance of incorporating tail risks into the assessment of the macroeconomic outlook and the conduct of monetary policy.

Initial impacts of the conflict in the Middle East on the trade balance

Full study in Portuguese [here](#).

- The shock raised oil prices, supporting the petroleum and derivatives trade balance given Brazil's structural surplus; early data show an increase in the balance, albeit smaller than suggested by simple estimates, due to stronger import price gains, particularly for diesel.
- Exports to the Middle East account for a limited share of the total (4.6% in 2025), constraining aggregate effects; however, the region is important for specific products such as poultry, corn and sugar, and recent declines in shipments reflect logistical disruptions.
- Brazil's reliance on imported fertilizers, with significant Middle East participation in nitrogen-based inputs, exposes the agricultural sector to the price shock, which has risen markedly and may offset short-term trade gains.
- The timing of the shock mitigates immediate effects on the 2026 crop, but the concentration of fertilizer imports in the second half of the year points to potential risks for the 2027 harvest, making outcomes dependent on the conflict's duration and intensity.

Impacts of the Middle East conflict on Central Bank surveys

Full study in Portuguese [here](#).

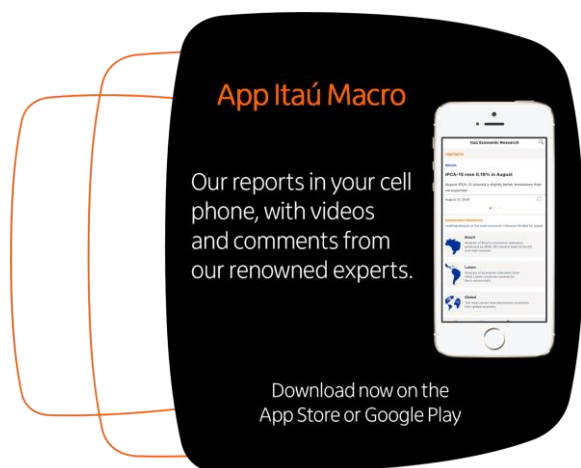
- The box consolidates the perceptions of market analysts and firms regarding the impacts of the Middle East conflict on Brazil, drawing on the Pre-Copom Questionnaire (QPC) and the Firmus Survey, with a focus on the transmission channels of the shock to inflation, activity, the external sector, and the fiscal stance.
- In the QPC, the prevailing assessment points to a relevant inflationary impact, with a median of 1.0 pp for the 2026 IPCA (largely already incorporated into projections) and short-term inflation surprises, including in items not directly affected by the shock — notably food at home. The effects on activity were perceived as small in the aggregate (median of 0.0 pp for 2026 GDP), but with high dispersion across responses; for the external and fiscal sectors, in turn, estimates pointed to a positive impact, of US\$10 billion on the trade balance and R\$20 billion on the 2026 primary result. In the Firmus Survey, around 80% of firms reported higher costs with oil derivatives, logistics, or transportation, with only partial pass-through to prices (43%) and a compression of expected margins over the next twelve months.
- Overall, the surveys converge on the reading that the conflict was perceived predominantly as an inflationary shock in Brazil, with limited impact on activity projections — a pattern that, in the QPC, diverges from what would be expected in a classical supply shock, while, in the Firmus Survey, the firm-level reading proved more consistent with this type of shock. It is worth noting that the data were collected before the signing, on June 17, 2026, of the memorandum of understanding to cease the armed conflicts in the Middle East.

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