

## Central Banks

## Fondeo rate unchanged at 3.0%. Relative monetary stance with respect to the US and the exchange rate on the spotlight

Iván Martínez Urquijo

---

**Banxico underlines the importance of strengthening the macroeconomic fundamentals as the exchange rate volatility rises, especially when FED's normalization process is expected soon**

- Possible adverse effects from a sustained peso depreciation join the relative monetary stance with respect to the US and the evolution of economic slack as the main factors that will draw particular attention from the central bank.
- Banxico sets 2015 as the deadline to achieve the convergence to inflation target.
- The balance of risks of inflation did not change significantly. The inflation slump during the first days of January was considered in line with expectations, while the risks of a protracted peso depreciation were highlighted.
- Downside risks on economic activity linger as the private consumption does not show clear recovery signals and as the contribution of public expenditure to economic growth is limited.
- The balance of risks for global activity impaired further as Japan and the Eurozone struggle with deflation pressures. In contrast the recovery of the US economy strengthens.
- Bottomline. The possible adverse effects on inflation from a prolonged peso depreciation led Banxico to adopt a cautious tone, especially as the beginning of FED's normalization process approaches. The current statement reinforces our perspective of a rate hike given the greater attention to the exchange rate and the relative monetary stance; and given the highlighting to the sound macroeconomic fundamentals. In short, given our base scenario of a 3.5% GDP growth and a year-end inflation around 3.0%, we maintain our expectation of a monetary pause until the third quarter of 2015.

Chart 1

Highlights from recent statements

	Dec-5th-14	Jan-29th-15	Bottom line*
Global context	<ul style="list-style-type: none"> <li>World economic growth <b>is still weak, but with differences across countries</b></li> <li>The US economic recovery strengthens</li> <li>The balance of risks of economic activity <b>impaired additionally</b></li> </ul>	<ul style="list-style-type: none"> <li>World economic growth <b>is still weak, but with differences across countries</b></li> <li>The US economic recovery strengthens</li> <li>The balance of risks of economic activity <b>impaired further</b></li> </ul>	<b>Mixed signals as US recovery continues</b>
Economic activity	<ul style="list-style-type: none"> <li>The <b>balance of risks impaired.</b></li> <li>Economic growth <b>moderated</b> during third quarter</li> <li>The economic slack prevails</li> <li>Private <b>consumption does not show signals of recovery. Public expenditure effects on growth are limited.</b></li> </ul>	<ul style="list-style-type: none"> <li>Downside risks to economic activity linger.</li> <li>Economic growth shows a <b>moderate recovery</b></li> <li>The economic slack prevails</li> <li>Private <b>consumption does not show signals of recovery. Public expenditure effects on growth are limited.</b></li> </ul>	<b>Dovish tone</b>
Inflation	<ul style="list-style-type: none"> <li><b>Upward risks increased</b></li> <li><b>Protracted peso depreciation is the major risk factor</b>, although it is <b>offset partially</b> by economic slack.</li> <li>It is estimated that headline inflation will be close to 3.0% from the first half of 2015 onward</li> <li><b>Upward expectations</b> of the <b>short-term real rate</b> even without any change of the reference rate.</li> </ul>	<ul style="list-style-type: none"> <li><b>Balance of risks with no major changes</b></li> <li><b>Protracted peso depreciation is the major risk factor</b></li> <li>Headline inflation in line with perspectives</li> <li>It is estimated that headline inflation will be at 3.0% around first half of 2015</li> </ul>	<b>Neutral tone</b>
Policy decision	0.00	0.00	
Rate	3.00	3.00	

\* Own interpretation based on the tone and wording of the Policy Statement

Source: BBVA Research based on monetary policy statements.

Disclaimer

This document was prepared by Banco Bilbao Vizcaya Argentaria's (BBVA) BBVA Research and BBVA Bancomer S. A., Institución de Banca Múltiple, Grupo Financiero BBVA Bancomer on behalf of itself and is provided for information purposes only. The information, opinions, estimates and forecasts contained herein refer to the specific date and are subject to changes without notice due to market fluctuations. The information, opinions, estimates and forecasts contained in this document are based upon information available to the public that has been obtained from sources considered to be reliable. However, such information has not been independently verified by BBVA Bancomer, and therefore no warranty, either express or implicit, is given regarding its accuracy, integrity or correctness. This document is not an offer to sell or a solicitation to acquire or dispose of an interest in securities.