

Central Banks

Banxico will stick to the monetary pause

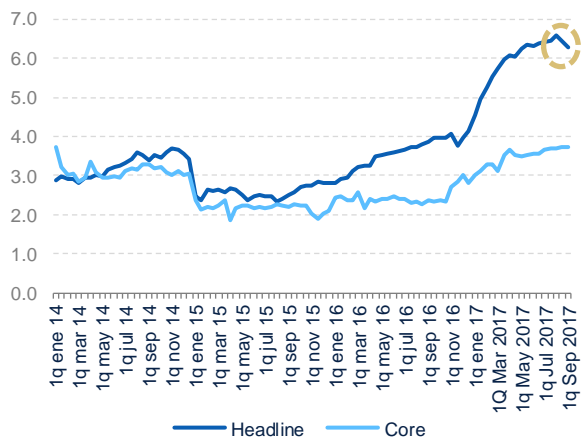
Javier Amador / Iván Martínez Urquijo / Carlos Serrano

27 September 2017

The next monetary policy meeting will be held on Thursday September 28th. We expect Banxico to hold the reference rate at 7.0% for the following reasons. First, recent inflation figures are consistent with central bank's expectations and communication. During the first fifteen days of September inflation declined with respect to its peak in August and it is expected to continue with this trend in the coming months. That is, as inflation reached its turning point, the convergence to the inflation target is underway, and that is exactly what Banxico has stressed recently with relation with its monetary stance, that the current level of the monetary policy rate is consistent with the convergence of inflation to the target in 2018. Second, given the expected path of inflation, monetary conditions will tighten with no need of further rate hikes. As the short rate remains on-hold and inflation declines, in the most probable scenario, the real rate will increase to levels not seen since 2009. The latter in a context of a stable exchange rate would lead to a gradual tightening of the monetary conditions. Third, the expected path of economic activity is consistent with the monetary pause. Eventhough the economic growth surprised to the upside during the first half of the year, recent consumption and industrial activity figures point to a slowdown in the coming quarters, making further rate hikes less consistent with the "efficient convergence" criteria. Finally, the more gradual than expected monetary normalization in the US and the low risk aversion environment give Banxico more degrees of freedom to manage its stance.

Going forward, in the most probable scenario, we expect the monetary policy rate to be on-hold until the second half of 2018. Banxico will maintain its restrictive current stance as inflation remains above the upper end of the interval around the inflation target. Similar to recent statements the tone will be mostly neutral but emphasizing that the central bank will follow closely inflation dynamics in order to be ready to act if any major deviation from its outlook arises.

Figure 1. Headline and core inflation
% YoY



Source: BBVA Research based on INEGI data

Figure 2. Monetary conditions index
Index



Source: BBVA Research

Disclaimer

This document has been prepared by BBVA Research at the Banco Bilbao Vizcaya Argentaria, S.A. (BBVA) and by BBVA Bancomer. S. A., Institución de Banca Múltiple and the BBVA Bancomer Financial Group, on their own behalf and is for information purposes only. The opinions, estimates, forecasts and recommendations contained in this document refer to the date appearing in the document, and, therefore, they may undergo changes due to market fluctuations. The opinions, estimates, forecasts and recommendations contained in this document are based on information obtained from sources deemed to be reliable, but BBVA does not provide any guarantee, either explicit or implicit, of its exactitude, integrity or correctness. This document does not constitute an offer, invitation or incitement to subscribe to or purchase securities.