

## Central Banks

# Fondeo rate unchanged at 3.0%. Neutral tone that denotes the pause will remain the rest of 2014

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## Encouraging US economic perspectives and domestic economic reforms offset the downside risks of the global economy. Inflation balance of risks unchanged.

- No changes on the balance of risks of domestic economic activity as encouraging US economic perspectives and domestic economic reforms offset the downside risks of the global economy. In fact, Banxico expects a “moderate recovery” of the Mexican economy in the third quarter.
- No changes on the balance of risks of inflation. Some upside risks linger such as a spike in financial markets volatility and a rise in minimum wage beyond inflation and expected productivity. On the contrary, a further decline of telecom prices represents a downside risk.
- Furthermore, the central bank stresses that the “recent social events” pose a downside risk on inflation as they could affect adversely the expectations of economic agents and therefore the pace of economic growth.
- The year-end inflation estimation remained at around 4.0%, however the convergence to the 3.0% level was delayed slightly as it was expected to take place sometime “during the first half of 2015” and now it is expected to happen “from the first half of 2015 onwards”. Regarding core inflation the year-end estimation close to 3.0% and under 3.0% for 2015 remained unchanged.
- As expected Banxico underlined the absence of lack of liquidity episodes in the exchange rate market during the recent spike of volatility.
- Bottom line. The communiqué denotes some confidence that the better than expected US economic figures will lead to a more dynamic domestic economy in the remaining two quarters, leaving aside negative surprises such as the one seen during the first three months of the year. Cautiousness remains on the inflation side as this indicator is still above 4.0% and some upside risks are still lurking. In short, based on Banxico’s efficient convergence to inflation criterion we consider that current economic perspectives are consistent with a monetary pause for the rest of the year.

Table 1  
**Highlights from recent statements**

	Sept-5th-14	Oct-30th-14	Bottom line*
Global context	<ul style="list-style-type: none"> <li>World economic growth <b>recovered</b> during the 2Q.</li> <li><b>US</b> Economic activity and employment <b>strengthened</b></li> <li>In balance, <b>downside risks</b> for world economic growth have <b>declined</b></li> </ul>	<ul style="list-style-type: none"> <li>World economic growth <b>denotes new signals of weakness</b></li> <li>Global slowdown and US dollar appreciation could <b>hamper US growth in 2015</b></li> <li>The balance of risks of economic activity <b>impaired</b></li> </ul>	<b>Less optimistic tone prompted by a slowdown in global growth</b>
Economic activity	<ul style="list-style-type: none"> <li>The balance of risks of economic activity <b>improved</b></li> <li>Domestic demand <b>recovered somewhat</b></li> <li><b>The economic slack prevails</b></li> </ul>	<ul style="list-style-type: none"> <li>The balance of risks of economic activity <b>remains unchanged</b></li> <li>A moderate recovery during 3Q is expected.</li> <li><b>The economic slack prevails</b></li> <li><b>US economic perspectives</b> and <b>structural reforms temper the impairment of the global growth</b></li> </ul>	<b>Neutral tone. Confidence in US economic perspectives</b>
Inflation	<ul style="list-style-type: none"> <li><b>Balance of risks impaired in the short run due to transitory factors</b></li> <li>Inflation is expected to close <b>2014 around 4.0%</b></li> <li>It is expected that headline inflation will be <b>close to 3.0% during the first half of 2015</b></li> </ul>	<ul style="list-style-type: none"> <li><b>Balance of risks unchanged.</b></li> <li>Telecom prices and recent social events: downside risks</li> <li>Financial volatility and minimum wage increases: upside risks</li> <li>It is estimated that headline inflation will be <b>close to 3.0% from the first half of 2015 onward</b></li> </ul>	<b>Cautious tone</b>
Policy decision	0.00		
Rate	3.00		

Source: BBVA Research based on Banxico's communiqués.

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