Central Banks

Banxico cuts its policy rate 50bp to 6.0% at an unscheduled meeting, as we anticipated

We expect Banxico to take the policy rate to 3.0% by year-end

Javier Amador / Carlos Serrano

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- **In an unanimous vote, Banxico lowered the policy rate by 50bp to 6.00%**
- **May's scheduled meeting was not canceled; another cut of at least 50bp will surely come at that meeting**
- **More aggressive easing is warranted; we expect a 3.0% policy rate by year-end**
- **In a separate statement, Banxico also announced a series of unprecedented and welcomed liquidity measures**

Further rate cuts and an easing monetary policy stance are warranted

Banxico lowered its policy rate by 50pb to 6.0% at an out-of-schedule meeting today. We were expecting this cut in April because Banxico was already well behind the curve and it did not make sense to wait until the next scheduled meeting May 14th). We were also expecting Banxico to not only bring forward to April its scheduled May meeting (as it did in March), but to add an out-of schedule meeting in April and keep the one scheduled in May.

As opposed to the statement in March in which Banxico announced that they were bringing forward the scheduled meeting for that month, there is no mention to that in today's statement. We think that is one positive aspect to highlight since there is still plenty of room for Banxico to cut rates and a faster easing pace is warranted and needed. The fact that they did not cancel May's meeting clearly signals that another rate cut of at least 50bp will come in May. Another welcome change in the statement is that the vote was unanimous, as opposed to March's decision, which signals that (finally) all Board members seem to see the need for more and faster easing.

Although the cut in April was only anticipated by six out of 25 analysts surveyed in the last Banamex survey released on April 3rd (the latest is set to be released later today), the cut is not surprising and widely expected by markets. The Mexican peso remained broadly unchanged following the decision, which should further ease Banxico's concerns as to the possible effects if they speeded up the easing pace.

Banxico acknowledged the rapidly deteriorating economic context but came short of acknowledging that the balance of risks to inflation is on the downside. In our view, there is no point to highlight inflation uncertainty in the current economic and inflation context as it might be counterproductive for inflation expectations (for more see). However, the wording of the statement and the inflation paragraph came much closer to our view on the economy and inflation, and signals that they will cut rates soon and will continue to cut going forward, barring a surprise increase of inflation or inflation expectations that we are not anticipating.

We have been arguing that Banxico should take the policy rate well below 5.0% this year, but the most hawkish and cautious Banxico's Board ever made us hesitate with our forecast. However, the growth scenario is rapidly deteriorating while the inflation scenario is clearly improving. At the same time, there is no point or need to keep high interest rates (for our rationale see). We forecast that Banxico will take the policy rate to 3.0% by year-end. Reaching the lowest policy rate on record is warranted.

In a separate statement, Banxico also announced a series of unprecedented moves to purchase securities and support financial market liquidity. All together, the measures totaled 750 billion pesos, or 3.3% of gross domestic product. This is also a needed and welcome development as we argued here. Measures included opening windows for repurchase agreements on government and corporate debt (as we recommended, see), as well as funding for commercial and government banks to support small businesses. These measures were badly needed and are a very positive development. They are not simulative for the economy as there is no quantitative easing involved, but they address the liquidity problem that may have eventually, sooner rather than later, develop into a credit crunch with possible solvency problems for some.

Together, today's steps and the implicit signal for the rate cut cycle represent a significant change a welcome development within the scope of Banxico. We still think that Banxico should continue to rapidly ease monetary policy since an easing stance is warranted. A more appropriate monetary policy stance would not only address the economy needs in terms of the scope of traditional monetary policy, but also reinforce liquidity measures and also potentially more widely open the door for expansionary policy if at some point in the near future the government realizes that it is urgent and appropriate. An e expansionary fiscal policy better suits the current needs of countercyclical economic policies, but further monetary policy easing is also needed