

Central Banks

We are changing our call for tomorrow's MPC decision to pause following today's unexpected strong core inflation print –rising above 4.0% YoY

This data likely marks the end of the easing cycle

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- Core inflation rose strongly, to 4.1%, in the first half of March
- The non-anticipated higher-than-expected core inflation print was driven by both core goods prices, and services prices, pushed upwards by a 15% increase in airfare prices as lockdown measures have relaxed and people seem to be disregarding pandemic-related risks
- Looking ahead, headline inflation is set to increase further in March and above 5.0% in April, while core easing is unlikely to occur until late 2Q
- If demand picks up and/or the reopening of the economy in spite of continued risks translates into higher prices, core inflation could remain sticky to the downside for longer than previously thought
- Overall, the inflation release changes our call for tomorrow's Monetary Policy Committee (MPC) meeting to pause at 4.0%
- The wording might signal data-dependent decisions going forward
- Yet, due to the fact that monetary policy operates with a lag, alongside the communication challenges that making more than one pause during an easing cycle would represent, we now think that the current easing cycle already ended with the monetary policy rate at 4.0%

We no longer expect Banxico to cut the monetary policy rate at tomorrow's meeting; the surprising jump in core inflation in the first half of March likely marks the end of the easing cycle

In today's inflation data release for the first half of March, core inflation jumped above 4.0% YoY (to 4.09%), surprising decisively to the upside (BBVA Research: 0.20% FoF, 3.91, same forecast as the consensus one). With this, both headline and core inflation stand at 4.1% i.e., above Banxico's 2-4% target range.

Up until this data –i.e., new information–, we thought that the arguments for a pause were not solid (for details [see](#)). Nevertheless, we assigned a high probability (40%) to a hold decision for three reasons not related with the current global and domestic backdrop. First, Banxico has a history of backward-looking decisions. Second, it also has a

tendency of being excessively cautious in our view. Third, to a degree, it seems to have some disregard for the importance of clear communication as an important policy tool.

However, today's core inflation print represents a game-changer in our view. Not only the MPC will most likely hold the monetary policy rate unchanged at 4.0%, but due to the fact that monetary policy operates with a lag, alongside the communication challenges of making more than one pause during an easing cycle, we now think that the current easing cycle already ended with the monetary policy rate at 4.0%

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