

Central Banks

Banxico will likely take the policy rate to 5.25% in December

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November 11, 2021

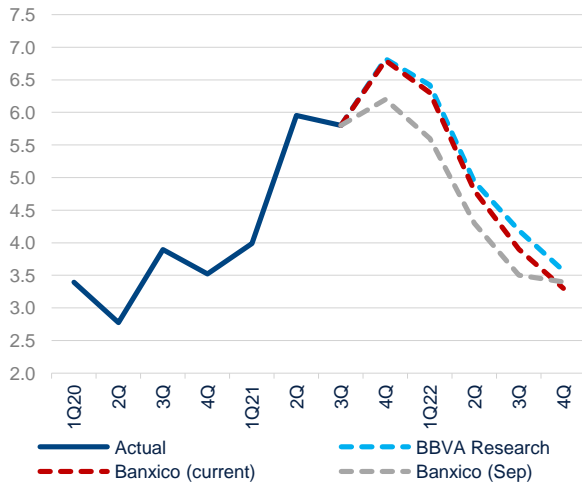
The probability of additional hikes in 1Q22 has increased

- **As we expected—and in line with the consensus forecast (7 out of 31 analysts predicted a rise of 50bp)—Banxico raised its benchmark rate 25bp to 5.00%.** Voting was again split, four to one, with the Deputy Governor, Gerardo Esquivel, once more voting to keep the rate on hold. The voting could be seen as a sign of a less hawkish attitude than had been anticipated, since none of the members voted for a bigger increase—forecast by 23% of analysts—and because one member continued to vote in favour of leaving the rate unchanged. The economic contraction in the third quarter of the year, which increased spare capacity, may also have influenced the decision.
- **The tone of the statement was similar to the last one, but contained a few tweaks which could be interpreted as hawkish. Despite that, there are no signs that Banxico is considering increasing the size of its rate hikes in the near future.** Banxico indicated that the shocks behind the major spike in inflation "are largely considered to be transitory", which is a slight change from the previous assessment —"it expected them to be temporary" i.e. it appeared to signal a certain risk that some of the factors that have driven up inflation may be of a more permanent nature — an almost identical modification to that made by the Federal Reserve. The statement went on to say that the horizon in which these shocks may continue to affect inflation "is unknown [and] they have involved a wide range of products, while being of considerable magnitude. This poses greater risks to the price formation process and to inflation expectations." These messages give the impression that Banxico considers it best to continue with its rate-hiking cycle. We expect a further 25bp rise to 5.25% in its December meeting.
- **The upward revision in the core inflation forecast gives an upward bias to our pause forecast after an additional 25bp rise to 5.25% in December.** Banxico considerably revised to the upside its short-term inflation forecasts and it is now projecting an almost identical trend for headline inflation to our own (see Figure 1); however, its core inflation forecast is for a further significant acceleration in 1Q22 (see Figure 2). If Banxico's latest core inflation forecasts materialize, the chances that three of the four members¹ who voted for 25bp rate hikes in the last two meetings could be inclined to continue doing so in 1Q22 are higher now. Having said that, additional preemptive hikes would not be particularly necessary so close to the inflation turning point with core inflation expected to start to ease in 2Q22. Therefore, Banxico's latest forecasts suggest that the likelihood of a rate hike above 5.25%—that we forecast for December—has increased.

¹ Banxico governor, Alejandro Díaz de León, the fourth member who voted to raise rates, will no longer be on the Governing Board after its first meeting next year — which is expected to take place in February

The current headline inflation trend projected by Banxico is now almost identical to our own...

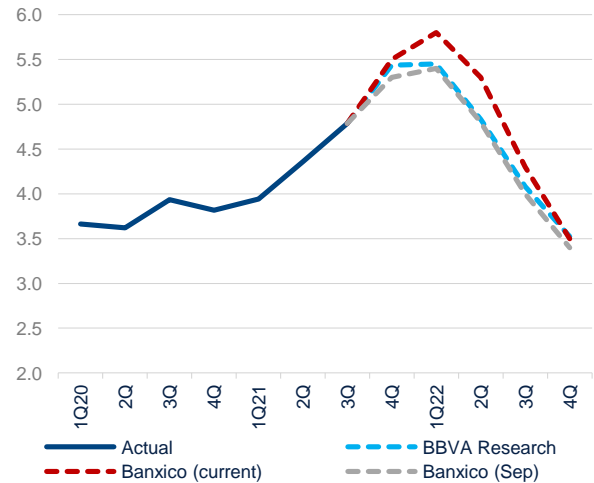
Figure 1. **HEADLINE INFLATION OUTLOOK (YOY % CHANGE)**



Sources: BBVA Research / Banxico / INEGI

... however, it forecasts that core inflation will rise further in 1Q22

Figure 2. **CORE INFLATION OUTLOOK (YOY % CHANGE)**



Sources: BBVA Research / Banxico / INEGI

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