

Central Banks

Banxico delivers third 50bp hike in a row

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The hiking cycle has much further to run, the question is whether Banxico will frontload the hikes or take a more gradual pace once core inflation starts to ease

- **Banxico raised the policy rate by 50bp to 6.50%.** The decision was not a surprise, not only because all analysts in the latest Banamex were expecting it, but also because President López Obrador (AMLO) revealed this decision earlier today. This is worrisome given that it means someone who was at the meeting revealed the decision, taken yesterday night. The decision was unanimous for the first time in this hiking cycle, with Mr. Esquivel, who had preferred smaller 25bp hikes in the last two meetings, now joining the other four members of the Board in voting for a larger hike. The fact that four of the five members of the Board chosen by AMLO are focused on Banxico's mandate eases concerns about the central bank's autonomy –it does not seem that AMLO wants to influence monetary policy. Moreover, he later apologized and added that he thought that the decision was already known to the public.
- **Banxico revised up sharply its inflation forecasts once again, bringing them close to our recently updated forecasts.** Banxico now expects headline inflation to ease to a 5.5% average in 4Q22 (up from 4.0%, and just slightly below our 5.6% projection) and core inflation to decelerate to a 5.2% average in the same quarter (up from 4.3%, and again, just a tad below our 5.3% projection). Banxico now expects headline and core inflation to drop to levels below 3.5% until 2Q23, compared to its previous forecast of 1Q23.
- **We expect inflation to remain well above 5.0% through year-end and core inflation to ease below 5.5% until Nov-Dec. Under this backdrop and with the hawkish shift by the Fed, acknowledged in the statement, the hiking cycle has much further to run.** We expect Banxico to take the policy rate to 8.0%. The question is Banxico will continue to frontload the hikes or take a more gradual approach once core inflation starts to ease. We expect core inflation this process to start in May, just after the next policy decision (May 12). For now, we think that Banxico will take a more gradual approach in coming meetings and shift back to 25bp hikes. Yet, if the Fed moves rates more aggressively at its next scheduled meeting (May 3-4) and/or core inflation accelerates further, Banxico might lean once again to lift rates by 50bp. Markets have already priced in a more hawkish view, while some analysts anticipate that Banxico will take the policy rate to 9.0%. It is important to note that given the global nature of the supply shocks affecting inflation, monetary policy will not be effective, as it cannot offset the shocks. Thus, we think that it is a better strategy for the central bank to front load hikes to avoid an unwelcome increase in long-term inflation expectations than to take a very restrictive stance at a moment when demand-side pressures are not driving higher inflation.

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