

Banxico Watch

Banxico held the policy rate steady for the second meeting in a row...

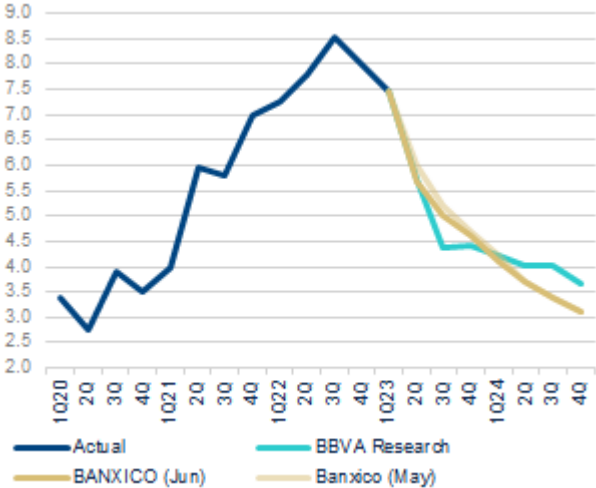
Javier Amador / Carlos Serrano
 June 22, 2023

... and repeated that it is set to keep it “at its current level for an extended period”

- Banxico**, in a unanimous decision, **kept the policy rate steady at 11.25%** for the second consecutive meeting **but kept a hawkish tone and reiterated that it is set to keep rates on hold for a while**. The decision was widely expected and there were no surprises in either the statement’s wording, which continues to strike a hawkish tone, or the changes to the inflation forecasts, which were only moderately adjusted to the downside. It reinforces our view that the tightening cycle has concluded. Earlier today, inflation figures for the first half of June were released. Headline inflation came down to a 27-month low and core inflation to a 15-month low after increasing less than our below-consensus forecasts in the first half of June. **Banxico acknowledged that the “disinflationary phase” remains underway, but stressed that the inflation outlook “will be complex and uncertain throughout the entire forecast horizon” and judged that the balance of risks remains biased to the upside.**
- As we anticipated (see), Banxico revised its 2023 headline inflation expected path downwards to bring it closer to our forecasts** (see Figure 1) and fine-tuned its short-term core inflation forecasts, adjusting to the downside this quarter’s forecast. We think that headline inflation is going to ease somewhat more rapidly than what Banxico expects in 2H23 (see Figure 1), but its average 4Q forecast (4.6%) is now closer to ours (4.4%). Banxico’s 2023 core inflation expected path remains broadly in line with ours (see Figure 2).
- Looking ahead, Banxico signaled that it will keep the policy rate unchanged for a while.** Banxico repeated that it will keep the policy rate “at its current level for an extended period”, moving to the sidelines in the coming meetings. The next move is not around the corner, but Banxico will shift to rate cuts after a long pause. The main question going forward is whether Banxico will keep rates steady throughout the remainder of 2023, allowing the real ex-ante rate to increase further (beyond 7.0-7.5%) given that inflation will not yet fall back to the target range, or will be forward-looking and start to cut the nominal policy rate in 4Q. With either option, **monetary policy will remain very tight in the foreseeable future. Yet, with falling inflation, well-anchored expectations, and a strong peso, we expect Banxico to start a rate cut cycle in 4Q23 to avoid an additional increase in the already very high ex-ante real rate, which is set to hover around 7.0% in the next few months.** Given that the peso strengthening, along with a very high monetary policy rate, has brought monetary conditions to restrictive territory, in a backdrop of falling inflation and expectations, after extending the pause during 2Q and 3Q, Banxico should start a rate cut cycle in 4Q to avoid a further tightening of the monetary policy stance, even if the Fed is still in a pause. A signal is not likely in the short term, but we continue to expect that Banxico will start to cut rates as soon as in November.

Banxico adjusted down its short-term inflation outlook, bringing it closer to ours...

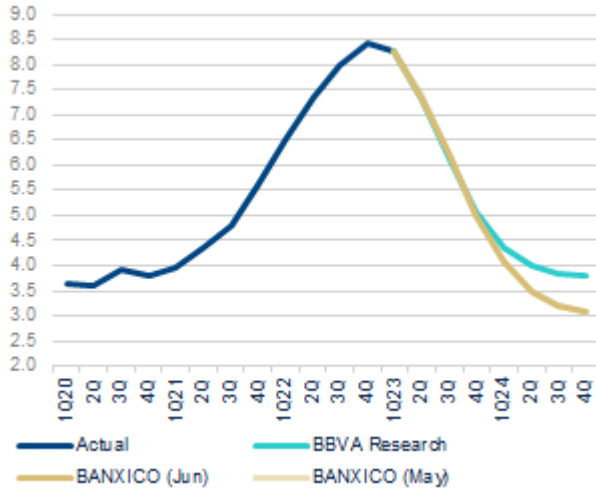
Figure 1. **HEADLINE INFLATION OUTLOOK**
(YOY % CHANGE, QUARTERLY AVERAGE)



Source: BBVA Research based on data by INEGI & BANXICO.

... and left its core inflation forecasts mostly unchanged, as we anticipated

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



Source: BBVA Research based on data by INEGI & BANXICO.

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