

# Banxico Watch

## México

November 29th 2011

### Análisis Económico

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## Preventive USD auction, that in addition supports a cut in fondeo rate... but surely not on friday

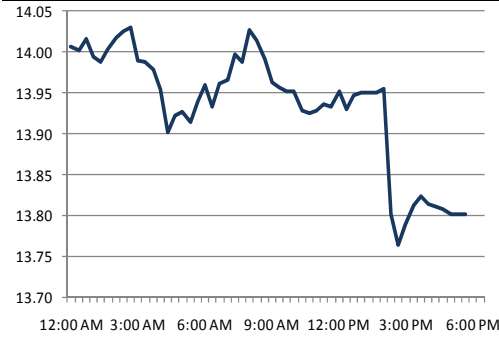
### Monetary policy decision of December the 2<sup>nd</sup>, 2011

- From November 30th onwards Banxico will offer USD 400 million daily through USD auctions when the exchange rate depreciates at least 2 percent with respect to the previous day. The peso appreciated around MXN 20 cents.
- The Exchange rate Commission reacts to slight signs of impairment in the Exchange rate market: wider bid-ask spread and lower operation volume
- Exchange rate appreciation supports BBVA Research perspective of a rate cut, though possibly not this Friday. A longer period is needed to evaluate the effect of this policy
- A lower volatility and level of the exchange rate in a well functioning market continue to be determinant factors for a rate cut, that we believe will take place in the first months of 2012

The Exchange rate Commission (Comisión de Cambios in spanish) will offer USD 400 million daily through USD auctions when the exchange rate depreciates at least 2 percent with respect to the previous day. This policy will provide liquidity to the exchange rate market and appreciate the peso. This policy intends to provide liquidity and preserve the well functioning of the domestic currency market. This seems to obey to a slight increase in the bid-ask spread and a reduction of operation volume (graphs 1 and 2). It is worth noting that previous interventions had the objective to normalize the market conditions.

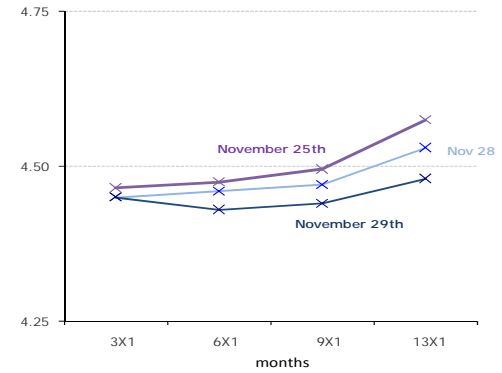
Recently, Banxico's communication has shown a dovish tone. However the central bank has stressed that high and volatile exchange rate is a risk for inflation, therefore the announcement of these USD auctions would increase the room for a rate cut, in line with BBVA Research perspective. Although we think that Banxico will cut the rate, this reduction could be delayed if the exchange rate market conditions impair. Besides, it is important to consider that the effect of a rate cut runs in the opposite direction to that of the USD auctions.

Graph 1  
Intraday Exchange rate. November 29th, 2011 (pesos per dollar)



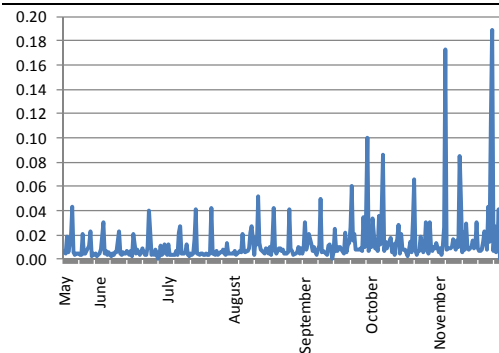
Fuente: BBVA Research

Graph 2  
Implicit Fondo rate in TIIE swaps



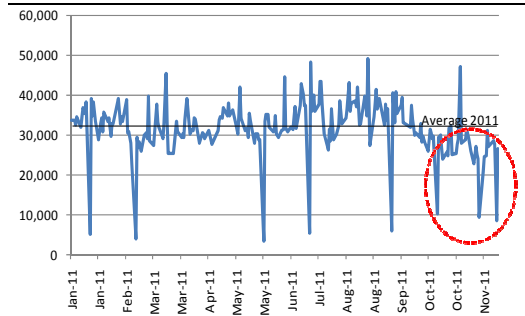
Fuente: BBVA Research and Valmer

Graph 3  
Exchange rate Bid - Ask spread (pesos per dólar)



Fuente: BBVA Research and Bloomberg

Graph 4  
Exchange rate operations. Spot and future markets (USD million)



Fuente: BBVA Research and Banxico

Aviso Legal

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