

Mexico Flash

Banco de México: Monetary policy rate on hold in the next meeting

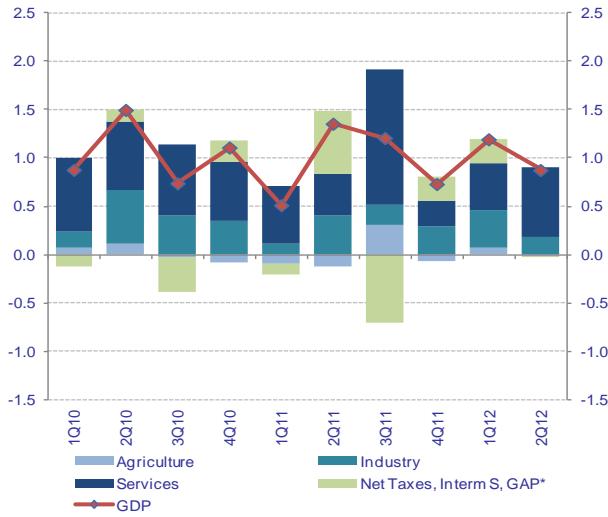
- The upward risks on inflation in the short term and to the downside in the medium term remain. The next announcements of the FED and BCE could contribute to reduce the risks on global activity.
- The monetary pause will continue in the rest of the year. The possibility of a rate cut continues if economic activity impairs given the existence of risk events.

Uncertainty remains on hold since last monetary policy meeting, while markets await monetary policy decisions by the FED and the ECB. It is true that at the end of July the expectation of a new round of monetary stimulus by the ECB reduced risk aversion, however, at present, there are still some doubts regarding the start date and the scope of this measure. Besides, the ruling on the constitutionality of the ESM by a German court next September 12th adds uncertainty to the situation in Europe. In the US, while recent data still points to deceleration, the slow recovery of employment has increased the possibilities of a new round of quantitative easing by the FED, even more after FED chairman expressed a deep concern about this situation.

On the domestic side, 2Q GDP figures surprised slightly upwards (0.9% q/q vs 0.7% q/q expected), but resulted below 1Q growth of 1.2% q/q. These figures confirm the moderate growth of the economy. It is worth noting that 2Q GDP growth was supported by internal demand. In particular, the services sector growth was 1.2% t/t, while external demand indicators still signal deceleration, even though the trend is positive. With respect to consumer prices inflation remains above 4.0% as a consequence of the price increase of grains, the bird-flu outbreak and the high prices of oil. In the short term a commodities price increase bias inflation risks upwards, however, given the slack in the economy there are not demand side pressures on prices and therefore, we consider that inflation will be below 4.0% in December. It is worth mentioning that the recent inflation surprise will lead to a positive comparison effect that will reduce the inflation level in the second half of 2013, given that supply shocks should have faded out.

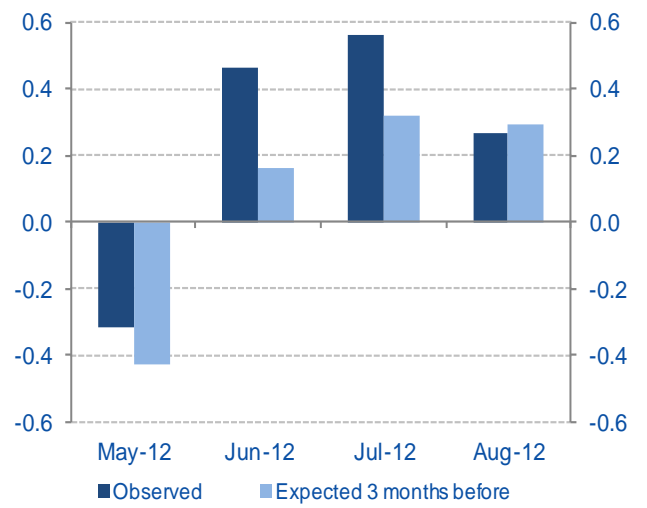
In sum, we consider that as the upwards risks on inflation and the downwards risks on global activity both remain, the conditions are consistent with a monetary pause during 2012. However a rate cut cannot be dismissed if domestic economic activity impairs.

Chart 1
México. GDP growth % q/q, and contributions



Source: BBVA Research INEGI

Chart 2
Inflation figures and expectations (% a/a)



Source: BBVA Research and INEGI

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