

Banxico – Unanimous 50bps hike given the renewed deterioration of the inflation outlook

- Today, Banxico’s Board decided to hike the reference rate by 50bps to 6.50% in a unanimous vote, in line with our call and consensus
- In our view, the tone of the statement and the direction of the individual votes suggest that the central bank maintains a very hawkish bias
- We also highlight:
 - (1) The revisions to all inflation forecasts, especially for 2022 but also for 2023. This implies that the expected convergence to the target was delayed by one quarter, to 1Q24;
 - (2) They removed the condition that the 50bps hike would be “...on this occasion...”, pointing to broader consensus; and
 - (3) We saw special concerns about the potential impact of the war in Ukraine on price dynamics, recognizing a high degree of uncertainty
- We reiterate our call of a 50bps hike in the May 12th decision. After this, we estimate five consecutive increases of 25bps, with the rate reaching 8.25% by year-end. For 2023 we see four 25bps hikes each, with a terminal rate of 9.25% at the end of June
- Long-term Mbonos still attractive, but MXN expensive

Banxico hikes 50bps. With this, the rate reached 6.50%, in line with our call and consensus. Contrary to recent decisions, the vote was unanimous. Just because of this, we believe the central bank has a more hawkish bias. However, it was reinforced with other details. Specifically, they recognized a more difficult environment in the face of "longer-lasting" inflationary pressures, "the intensification" of geopolitical turmoil –due to the conflict in Ukraine– and "greater" adjustments in monetary and financial conditions –mainly because of the Fed, which could accelerate its own hiking pace–. As a result: (1) Inflation forecasts were adjusted again for both components and through all of the forecast horizon (see table below); (2) the estimate for the convergence to the target was delayed to 1Q24; and (3) they confirmed that the balance of risks has deteriorated and is skewed to the upside. Comments on growth were minimal, suggesting the strong focus on price dynamics. Considering the individual votes and these details, we continue seeing +50bps on May 12th and five additional hikes of 25bps each, with the rate reaching 8.25% by the end of this year.

CPI forecasts

% y/y, quarterly average

	4Q21	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23	4Q24
CPI										
Current	7.0*	7.2	6.9	6.1	5.5	4.5	3.4	3.2	3.2	3.1
Previous	7.0*	6.9	5.4	4.6	4.0	3.4	3.2	3.1	3.1	--
Difference (bps)	--	30	150	150	150	110	20	10	10	--
Core										
Current	5.6*	6.5	6.7	5.9	5.2	4.1	3.4	3.1	3.1	3.0
Previous	5.6*	6.4	6.1	5.1	4.3	3.3	2.9	2.7	2.7	--
Difference (bps)	--	10	60	80	90	80	50	40	40	--

Source: Banco de México. *Observed data

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Winners of the award for best economic forecasters for Mexico in 2021, granted by Refinitiv



Banxico's 2022 policy decisions

Date	Decision
February 10	+50bps
March 24	+50bps
May 12	--
June 23	--
August 11	--
September 29	--
November 10	--
December 15	--

Source: Banxico

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The inflation outlook deteriorates further. Returning to some of the concerns of the [Quarterly Report](#) (QR), Banxico highlighted challenges from the war in Ukraine, representing greater uncertainty and inflationary pressures. This affected inflation forecasts and the balance of risks. On the former, the headline showed an average adjustment of +120bps in 2022 (with +150bps from 2Q22 to 4Q22) and +38bps in 2023, with the convergence to the target delayed by one quarter, to 1Q24. The core was moved by +60bps this year and +53bps in 2023. Although these adjustments were substantial, the path remains low. We believe this will force the central bank to carry out additional upward revisions and extend the tightening cycle at the same speed at least in the next decision. Lastly, the balance of risks remains deteriorated and skewed to the upside (similar to the QR), in our opinion with greater conviction regarding the impact of the conflict.

The hiking cycle will continue the rest of the year, with at least an additional +50bps in a more complex backdrop. We believe the vote's direction, overall tone of the statement, the revision of estimates, the evolution of the conflict, and global monetary policy, validate our view that Banxico will increase the rate by 50bps on May 12th. After this, we anticipate 25bps each in the five remaining decisions of the year (June, August, September, November and December), taking the rate to 8.25%. Our estimates are based on: (1) A more complex price outlook, with [our forecasted path](#) almost +110bps for 4Q22 average annual inflation vs. the one from the central bank; (2) a more hawkish Fed, also raising the *Fed funds* rate in all decisions this year and without ruling out that it could accelerate the pace to +50bps in the short-term; and (3) the possibility of a greater deterioration in global financial conditions and/or more shocks to inflation (*e.g.* due to an upsurge of the armed conflict, new disruptions because of the virus and even pass-through from rising inflation expectations, among others). In this sense, the risk is that Banco de México could decide to tighten even faster than the current pace. Therefore, we will continue paying close attention to the institution's publications to assess the changes in the environment, especially in the face of uncertainty due to the conflict and its ramifications in terms of economic policies.

From our fixed income and FX strategy team

Long-term Mbonos still attractive, but MXN expensive. After the decision, short-term nominal rates did not react much as markets had already discounted +50bps. However, long-term Mbonos extended the selloff by 3bps and adjusted +12bps on average. This shift caused the curve to steepen, partially moderating the inversion of the curve in the 3s10s to -7bps from yesterday's all-time low of -15bps. TIEE-28 IRS reflected few changes, gaining 3bps in the short-end and pressured by 5bps in the long-end. The market is still pricing-in aggressive moves, accumulating implied hikes of +303bps this year (including today's +50bps). In terms of strategy, long-term Mbonos still look attractive. However, high volatility limits room for directional trades. On FX, the Mexican peso strengthened to 20.09 from 20.15 per dollar, extending the appreciation trend of the last 10 days which has been supported by an attractive carry. Despite of this, we see limited room for further gains considering a fair value of 21.02 according to our REER model and net shorts in the peso. In this sense, we see the 20.00-20.10 area as attractive for buying USD with a medium-term horizon.

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We, Alejandro Padilla Santana, Juan Carlos Alderete Macal, Alejandro Cervantes Llamas, Manuel Jiménez Zaldivar, Marissa Garza Ostos, Francisco José Flores Serrano, Katia Celina Goya Ostos, José Luis García Casales, Yazmín Selene Pérez Enríquez, José Itzamna Espitia Hernández, Carlos Hernández García, David Alejandro Arenas Sánchez, Paola Soto Leal, Víctor Hugo Cortes Castro, Hugo Armando Gómez Solís, Daniela Olea Suárez, Miguel Alejandro Calvo Domínguez, Luis Leopoldo López Salinas, Leslie Thalía Orozco Vélez, Gerardo Daniel Valle Trujillo and Isaías Rodríguez Sobrino, certify that the points of view expressed in this document are a faithful reflection of our personal opinion on the company (s) or firm (s) within this report, along with its affiliates and/or securities issued. Moreover, we also state that we have not received, nor receive, or will receive compensation other than that of Grupo Financiero Banorte S.A.B. of C.V for the provision of our services.

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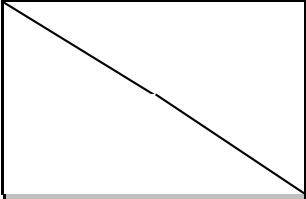
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