

## Banxico minutes – Hiking cycle not necessarily over and cautious stance towards rate cuts ahead

- Banxico just published the minutes of the meeting held last April 12, in which the board of governors unanimously decided to maintain the reference at 7.5%
- We perceived a slightly more hawkish tone vs. market expectations as we consider that the monetary authority has not signaled that the hiking cycle is over yet
- We find a very extensive discussion regarding the implications of U.S. Fed monetary policy normalization on investment flows and the destabilizing effect it could have on financial markets, particularly in emerging economies.
- In addition, most of the board members agreed that cyclical conditions remain tight, highlighting the effort made by the central bank for its measurement (consumption, economic activity, labor market, and credit), which precisely confirm the reading of the output gap in the sense that there is no slack left in the economy
- Regarding inflation, some members alluded to its downward trend. Nevertheless, one member emphasized that “...it seems premature to conclude that the process of decreasing inflation is already consolidated...”
- Moreover, the Board commented that the balance of risks for inflation is tilted upwards amid a highly uncertain environment. However, some highlighted that “... the bias is less steep with respect to the previous monetary policy decision ...”
- In addition, we highlight that one board member emphasized that: “...even considering a scenario of i) a gradual normalization of monetary policy in the U.S., ii) a stable macroeconomic environment in Mexico [...]; and iii) a favorable outcome NAFTA renegotiation, Banxico should not give an image of complacency that could imply that in the near future it might be able to reduce the reference rate ...”
- The minutes continue to support our view that Banxico could hike once again sometime in 2Q18, subject to incoming inflation and economic activity data, as well as to FX behavior and volatility conditions in domestic and international financial markets
- Looking ahead, we believe that the central bank has room to cut the reference rate by 50bps, as uncertainty ebbs away

April 26, 2018

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*From our fixed income and FX strategy team*

- **Local rates are paring recent gains following Banxico's modest hawkish tone within today's minutes, suggesting a strong likelihood of larger term and risk premiums in coming months. In terms of strategy, we suggest investing in floating-rate securities while awaiting better market conditions in order to implement long strategies in the mid-end of the Mbonos curve (for foreign investors) and long-duration Mbonos (for local participants)**
  
- **The Mexican peso is falling 0.2% with respect to yesterday's close, trading at 18.89 per dollar. In our view, this is driven by dollar strength in the last hour more so than this release. In this sense, it is our take that Banxico's signal of prudence because of the possibility of higher volatility will continue to support the currency. In spite of the latter, we remain cautious and with a long USD/MXN bias for intraday trading, expectation further pressures in the currency during 2Q18 as we estimate that the risk premium is modest**

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