

Ahead of the Curve

November 11, 2016

Market focus this week will on Banxico's monetary policy announcement

- **Banxico's monetary policy announcement.** On Thursday, Banxico will hold its eighth policy meeting of the year. The monetary policy *communiqué* will be published at 2:00pm (EDT). We believe that board members will increase the reference rate by 75bps to 5.5%. We consider that the depreciation of the Mexican Peso, derived from Donald Trump's victory on Tuesday's election will force the decision of the central bank

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Mexico weekly calendar

DATE	TIME (EDT)	EVENT	PERIOD	UNIT	BANORTE-IXE	CONSENSUS	PREVIOUS
Tue 15-Nov	10:00am	International reserves	11-Nov	US\$ bn	--	--	175.1
Tue 15-Nov	12:30pm	Government weekly auction: 1-, 3-, and 6-month Cetes; 3y MBono (Dec'19); 3y Udibono (Jun'19)					
Wed 9-Nov	2:00pm	Banxico's monetary policy decision	October	%	5.50	5.25	4.75

Source: Banorte-IXE; Bloomberg

Proceeding in chronological order...

Weekly international reserves report. On Tuesday, at 10:00am (EDT), Banco de Mexico will release its weekly balance report. Last week, net international reserves increased by US\$177 million amounting to US \$175.2 billion on November 4. According to Banxico's report, this figure comes mainly as a result of: (1) Dollar purchases by Banxico to the Federal Government for US\$1,927 million; along with a (2) US\$1,751 million increase of the short term government liabilities. In this context, the Central Bank's international reserves have diminished by US\$1,467 million this year (please refer to the table on the next page).

Banxico's foreign reserve accumulation details

US\$, million

	2015	11/04/16	11/04/16	Year-to-date
	Balance		Flows	
International reserves (B)-(C)	176,735	175,267	177	-1,467
(B) Gross international reserve	177,597	178,909	1,927	1,312
Pemex	--	--	-86	2,732
Federal government	--	--	2,157	1,710
Market operations	--	--	0	-5,562
Other	--	--	-143	2,433
(C) Short-term government's liabilities	861	3,641	1,751	2,779

Source: Banco de México

Weekly government bond auction. Also on Tuesday, the Ministry of Finance (MoF) –via Banco de Mexico as its financial agent-, will offer 2-year fixed-rate Mbonos (Dec’19), 3-year inflation-linked Udibonos (Jun’19), in addition to the “more traditional” 1-, 3-, and 6- month zero-coupon Cetes (please refer to the table below). As usual, the results will be released at 12:30pm (EDT).

Auction specifics (Tuesday, November 15, 2016)

	Maturity	Coupon rate, %	To be auctioned ¹	Previous yield ²	
Cetes					
	1m	15-Dec-16	--	7,000	4.81
	3m	16-Feb-17	--	11,000	5.07
	6m	11-May-17	--	12,000	5.03
Mbono					
	20y	11-Dec-19	5.00	9,500	5.50
Udibono					
	30y	13-Jun-19	4.00	850	2.22

Source: Banorte-Ixe with data from Banco de México

1. Except for Udibonos, which are expressed in UDI million, everything else is expressed in MXN million. 2. Yield-to-maturity reported for Cetes, Mbonos and Udibonos

We expect a 75bps rate hike. On Thursday, Banxico will hold its eighth policy meeting of the year. The monetary policy *communiqué* will be published at 2:00pm (EDT). We believe that board members will increase the reference rate by 75bps to 5.5%. We consider that the depreciation of the Mexican Peso, derived from Donald Trump’s victory on Tuesday’s election will force the decision of the central bank

Within the *communiqué*, the central bank will probably emphasize on the following issues: (1) The balance of risks for inflation in the horizon, in which monetary policy operates, has continued to deteriorate, highlighting the considerable depreciation of the MXN; (2) A higher probability of financial volatility on the back of economic policies Donald Trump could enact; and (3) The necessity to adapt Banxico’s monetary policy in order to prevent that the depreciation of the Mexican currency and the adjustment in relative prices translate into a deterioration of inflation expectations

Even though Mexico’s headline CPI index has remained below Banxico’s 3% target, we believe that the balance of risks for inflation has deteriorated. The last inflation reports have shown a higher pass-through effect from MXN to prices, which has been observed in the upward trend of the core index, particularly on goods prices. Moreover, the depreciation of the MXN since Donald Trump’s victory could generate pressure not only on the consumer price index, but on inflation expectations on the medium and long-term.

Moreover, Banxico has strongly highlighted the importance of keeping inflation expectations firmly anchored in line with its 3% target. In fact, most of the board members agreed that the 50bps hike in September was justified by the significant depreciation of the Mexican currency, and its potential negative impact on inflation expectations.

Although we expect Donald Trump's victory to have a negative impact on the Mexican economy (*for further information refer to our research note: "The world after November 8th – Revising our macroeconomic framework for 2017-2018" <[pdf](#)>*), current levels of USD/MXN on top of demand side pressures could trigger a disorderly behavior of inflation in the coming months.

The board members have shown complacency with monetary policy actions, which have been effective in order to improve the balance of risks to inflation. In this sense, we consider that Banxico will increase another 75 bps in the reference rate in December, leaving it at 6.25% by year-end. The minutes of this meeting will be published on December 1, and the next monetary policy announcement will take place on the December 15th.

Disclaimer

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