

## Banxico Minutes – High uncertainty justifies a prudent stance

- Banxico published the minutes of the meeting held on November 14<sup>th</sup>, in which the Board of Governors cut the reference rate by 25bps, to 7.50% in a majority decision
- The dissenting votes were cast, once again, by Deputy Governors Gerardo Esquivel and Jonathan Heath
- In our view the tone was dovish, similar to the communique and yesterday's 3Q19 *Quarterly Report*
- As in the QR, comments on growth were almost entirely dovish, as reflected in the downward adjustment in the central bank's GDP estimates across the forecast horizon
- We highlight an interesting debate about the balance of risks for inflation, in which high uncertainty about the outlook for prices, both in the short- and mid-term, seem to justify to continue easing in a prudent manner
- We also noted that most members saw lower financial stability risks, both global and domestic, particularly about the market reaction to recent actions on Pemex
- Comments about the relative monetary policy stance suggest that Banxico will indeed decouple from the US Fed
- We maintain our view of a 25bps rate cut in December, to 7.25%, extending into 2020 with an additional 125bps of easing, likely front-loaded during the first half and with the reference rate closing next year at 6.00%
- The tone of the minutes is aligned to the market's perception of future actions from the central bank

**Banxico in easing mode.** Banxico just published the minutes of the meeting held on November 14<sup>th</sup>, in which the Board cut the reference rate by 25bps to 7.50%, in a majority vote (3-2). In our view the tone is dovish, similar to the communique and yesterday's *Quarterly Report* (QR), in which we saw downward revisions in GDP estimates for 2019 and 2020 and a slightly better outlook for headline inflation in the short term. For details, see: "*Banxico QR – Lower growth estimates reinforce the dovish bias*", <[pdf](#)>. Overall, we highlight that the document suggests that virtually all members believe it is adequate to continue reducing the reference rate. Nevertheless, high levels of uncertainty, especially about the outlook for inflation and other global and domestic risks, justify the need to continue easing at a gradual pace.

**Gerardo Esquivel and Jonathan Heath were, once again, the dissenters.** In line with the previous decision, both favored a 50bps cut. Gerardo Esquivel kept his reasons largely unchanged relative to the previous meeting, highlighting two additions: (1) The reduction of some risks, both domestic and external; and (2) a restrictive monetary stance despite inflation hovering around the target, which is the only case in Latam.

November 28, 2019

www.banorte.com  
@analisis\_fundam

**Gabriel Casillas**  
Chief Economist and Head of Research  
gabriel.casillas@banorte.com

**Delia Paredes**  
Executive Director of Economic Analysis  
delia.paredes@banorte.com

**Juan Carlos Alderete, CFA**  
Senior Economist, Mexico  
juan.alderete.magal@banorte.com

**Francisco Flores**  
Economist, Mexico  
francisco.flores.serrano@banorte.com

### Fixed income and FX Strategy

**Alejandro Padilla**  
Head Strategist – Fixed-Income and FX  
alejandro.padilla@banorte.com

**Santiago Leal Singer**  
Fixed-Income and FX Strategist  
santiago.leal@banorte.com

**Leslie Orozco**  
Fixed Income and FX Strategist  
leslie.orozco.velez@banorte.com

Document for distribution among public

In addition, we highlight he said that “...*Under the current economic conditions, a 25-basis point reduction is not enough and comes in too late...*”. Jonathan Heath also kept most of his arguments largely untouched, adding emphasis on the relative monetary stance, pointing that there has not been any effective easing as other central banks have also cut rates. In this sense, he argued that “...*there is a wide margin of maneuver for the proposed reduction...*”. Overall, we consider that if a similar scenario to the current one prevails, both Deputy Governors will continue pushing for 50bps reductions in coming meetings.

**Are we in an easing cycle?** Considering the arguments of the dissenters and the document as a whole, we believe that we are indeed in an easing cycle, with the debate among members mostly about the pace but not its direction. In particular, we highlight one member’s comment stating that “...*the forward guidance on the monetary policy adjustment cycle should be subject to what the margins of absolute and relative monetary policy stances suggest, as well as incoming data and unexpected events...*”. Moreover, the majority agreed that, under the current environment of high uncertainty, it must be conveyed that monetary policy will adjust prudently, contributing to an orderly and sustained convergence of headline inflation to the 3% target. In our view, these comments (particularly the words “cycle” and “adjust”) and the bias of recent decisions, suggest that virtually all members see further rate cuts in the horizon, although the magnitude will depend on the outcome of certain events, including those about global monetary policy, financial stability risks, inflation and growth dynamics, among the most relevant.

**Economic activity still in stagnation, with concerns for the rest of 2019.** As reflected by revisions to estimates in yesterday’s QR, there already was a low bar for growth by the time of the meeting, driven by the 3Q19 GDP print. In this front, we observed a more detailed discussion in yesterday’s document, outlining clearly the reasons behind these adjustments. In this respect, we highlight that one member voiced concerns about the recent trend in services, adding that “...*stagnation throughout 2019 (...) is a cause for concern...*”. Looking further ahead, we also note an opinion about potential GDP, stating that: “...*weakness of gross fixed investment has had considerable implications for the evolution of the economy’s capital stock and that its growth rate is estimated to intensify in 2019 the downward trend it has been showing over the last years, with the consequent risks for potential growth...*”. We believe this may be one possible driver behind the magnitude of the revision lower for 2020 and a relatively muted estimate for 2021, and the additional widening of the output gap. Regarding the balance of risks, and as outlined yesterday, it still biased to the downside, with the approval of USMCA potentially having either a positive or negative impact depending on the outcome.

**Hot debate about the balance of risks for inflation.** Recent communications have avoided characterizing if the balance of risks is tilted to the upside, neutral, or tilted to the downside. In our view, this is a direct result of high uncertainty about the outlook, both in the short- and medium-term, a statement which was agreed upon by the majority. In this respect, the minutes shed light about the factors behind differences in opinion among Board members.

One member stated that the balance is *equilibrated* in the short-term, but in a longer horizon could be more uncertain as dynamics have been characterized by very low inflation at the non-core level coupled with resistance to the downside at the core. Another argued this is not the case even in the short-term, given risk factors such as Pemex's financial situation and wage policy. He/she added that although the room to cut has to be taken advantage of, it should be done cautiously given these risks. Some comments were also made about prevailing uncertainty over the magnitude of the minimum wage adjustment for 2020. One said that considering the negative output gap, a stronger MXN relative to 2018, negative annual growth in energy prices, and a modest increase in agricultural goods prices, wages seem to be the variable contributing the most to the resistance to the downside of core inflation. Given expectations of further increases, this resistance could prevail even with lower levels of activity. On the other hand, some stressed that a modest increase in headline inflation is expected in 1Q20 as a result of base effects, calendar effects, and seasonality—already reflected in yesterday's updated forecasts within the QR—. Another said the balance of risks is complex but, in his view, skewed *to the upside*. One judged it as *neutral* given a substantial decline in risks during the year, mainly on the back of an improvement in global financial conditions.

All in all, we believe this backdrop and differences suggest that monetary policy adjustments will be cautious, gradually incorporating the latest information available and responding to evolving economic conditions. In our view, the majority of Board members is following what we have dubbed as “data-and-events” dependency mode.

**Overall risks have diminished, but they are still present.** On the external front, most members argued that trade tensions between the US and China had diminished, coupled with a lower probability of both a hard *Brexit* and higher trade tensions. Moreover, they said that a series of actions by global central banks have helped reduce financial market volatility. Nevertheless, risks for the global economy prevail, associated with trade and geopolitical factors, along political and social uncertainty in some countries. On the domestic side, the main comments were about Pemex and public finances. For the former, they recognized the recent refinancing of external liabilities, recognized as favorable by the market. Nevertheless, there are some lingering concerns on this front, as “...*the majority warned about Pemex's business plan continuing to be a cause of concern for the rating agencies...*”. Regarding public finances, there were more mixed comments, with one member saying that weakness in public revenues could generate pressures, while another praised the financial stance of the federal government.

**The document reaffirms that Banxico will decouple from the Fed.** As usual, the Board commented on recent monetary policy decisions from other central banks, with most members stating that they do not expect additional adjustments in the Fed's stance. In this context, there was a concerted effort to make clear that our country's monetary policy does consider the Fed's actions, but "*...they are not a determinant for monetary policy decisions...*". This matches with the adjustments seen in the 'factors to consider' section in the statement as well as in some comments by several members. In this regard, one member referenced the easing cycles of other EMs, such as Brazil and Chile, which would allow for a greater degree of monetary easing.

**There seems to be two sets of views within the board.** When cross-referencing some comments scattered across the document with the part in which Esquivel and Heath outlined their arguments, it's relatively easy to identify when they diverge from the rest of the board. Both Deputy Governors build their case with some of the reasons previously outlined, while adding some factors such as greater economic slack and the recent behavior of inflation to push for a higher cut of the reference rate. On the contrary, the broad consensus between Governor Díaz de León along with Deputy Governors Irene Espinosa and Javier Guzmán, seems to point to the need of a prudent stance, with gradual adjustments. In particular, one of them stated that the level of the reference rate allows for the gradual reduction of the restrictive stance. Another commented that despite the deterioration in the growth outlook, there is still persistence to the upside in inflation expectations as well as uncertainty about other risks factors, allowing for some reductions in the reference rate but only in a cautious manner. Finally, the remaining member stated the monetary stance should adapt to the current environment gradually, considering risks and vulnerabilities the economy is experiencing and could face in the future. All in all, the position outlined by these three members, as well as their voting patterns relative to those of Esquivel and Heath, leads us to believe that 25bps cuts will continue to prevail.

**We expect Banxico to continue easing in 25bps steps.** In particular, we reiterate our call of a 25bps rate cut in December to 7.25%, extending into 2020 with an additional 125bps of easing, likely front-loaded during the first half and with the reference rate closing next year at 6.00%. Moreover, we are more confident that the pace of easing will be in 25bps clips as high uncertainty is likely to remain. In our view, the difference in opinions about the most convenient magnitude of rate cuts will continue to be the main focus. In this respect, we do not rule out entirely a future shift, which will depend mainly on the evolution of inflation dynamics and other risk factors, particularly as these could have an important effect in financial conditions and variables such as the Mexican peso, CDS levels, and local interest rates. Therefore, in our base case scenario the central bank will continue its easing cycle, carried out in a prudent manner.

*From our Fixed income and FX strategy team*

**The tone of the minutes aligned to the market's perception of future actions from the central bank.** The minutes from the last monetary policy decision from Banco de México have provided relevant information regarding the discussions around the last rate cut two weeks ago, where the benchmark rate was reduced to 7.50%. Minutes revealed, as expected, Deputy Governors Heath and Esquivel as the dissenter voters, leaning for a 50bps rate cut. All in all, the tone denoted in these minutes was consistent with the dovish bias conveyed in the communiqué and yesterday's Quarterly Report, with special stress in the local growth dynamics in light of the most recent data. The local fixed-income market depicted few reactions in the aftermath of this Thursday's release in a context where, in spite of thin liquidity on the back of the U.S. holiday, risk appetite remains cautious. In this sense, the yield curve's pricing holds its bets for stimulus policies from Banxico extending, pricing-in implied rate cuts of 26bps for this year-end and 128bps for 2020, in line with our expectation of a 25bps rate cut on December 19<sup>th</sup> and a reference rate closing 2020 at 6.00%. In terms of strategy and considering a foreign backdrop which has remarkably affected local rates' performance, we prefer to wait for better entry levels and market conditions for new directional recommendations.

Regarding to the FX market, the Mexican peso is falling 0.6% to 19.65 per dollar, finishing a week that has extended the pressures seen throughout November, reaching new fresh lows not seen since October 3<sup>rd</sup>. The peso has held a less fragile performance relative to other EM pairs, though it prints a 2.1% monthly sell-off against the USD. In our view, volatility associated with foreign geopolitical premiums will combine with the currency's implied rate diluting as a result of Banxico's cuts, holding a pressured trajectory for the USD/MXN going forward. In this sense, we recently took profits to our short-term tactical recommendation on USD longs at the 19.50 handle, now looking for new attractive entry points for similar trade ideas. In technical terms, the peso will find short-term supports the 19.75 area, with the main resistance being the 200-day MA at 19.27.

**Disclaimer**

The information contained in this document is illustrative and informative so it should not be considered as an advice and/or recommendation of any kind. BANORTE is not part of any party or political trend.

## Analyst Certification

We, Gabriel Casillas Olvera, Delia Maria Paredes Mier, Alejandro Padilla Santana, Manuel Jiménez Zaldivar, Tania Abdul Massih Jacobo, Katia Celina Goya Ostos, Juan Carlos Alderete Macal, Víctor Hugo Cortes Castro, Marissa Garza Ostos, Miguel Alejandro Calvo Domínguez, Hugo Armando Gómez Solís, Gerardo Daniel Valle Trujillo, José Itzamna Espitia Hernández, Valentín III Mendoza Balderas, Santiago Leal Singer, Francisco José Flores Serrano, Luis Leopoldo López Salinas, Jorge Antonio Izquierdo Lobato, Eridani Ruibal Ortega and Leslie Thalía Orozco Vélez, 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.

## Relevant statements.

In accordance with current laws and internal procedures manuals, analysts are allowed to hold long or short positions in shares or securities issued by companies that are listed on the Mexican Stock Exchange and may be the subject of this report; nonetheless, equity analysts have to adhere to certain rules that regulate their participation in the market in order to prevent, among other things, the use of private information for their benefit and to avoid conflicts of interest. Analysts shall refrain from investing and holding transactions with securities or derivative instruments directly or through an intermediary person, with Securities subject to research reports, from 30 calendar days prior to the issuance date of the report in question, and up to 10 calendar days after its distribution date.

## Compensation of Analysts.

Analysts' compensation is based on activities and services that are aimed at benefiting the investment clients of Casa de Bolsa Banorte and its subsidiaries. Such compensation is determined based on the general profitability of the Brokerage House and the Financial Group and on the individual performance of each analyst. However, investors should note that analysts do not receive direct payment or compensation for any specific transaction in investment banking or in other business areas.

## Last-twelve-month activities of the business areas.

Grupo Financiero Banorte S.A.B. de C.V., through its business areas, provides services that include, among others, those corresponding to investment banking and corporate banking, to a large number of companies in Mexico and abroad. It may have provided, is providing or, in the future, will provide a service such as those mentioned to the companies or firms that are the subject of this report. Casa de Bolsa Banorte or its affiliates receive compensation from such corporations in consideration of the aforementioned services.

Over the course of the last twelve months, Grupo Financiero Banorte S.A.B. C.V., has not obtained compensation for services rendered by the investment bank or by any of its other business areas of the following companies or their subsidiaries, some of which could be analyzed within this report.

## Activities of the business areas during the next three months.

Casa de Bolsa Banorte, Grupo Financiero Banorte or its subsidiaries expect to receive or intend to obtain revenue from the services provided by investment banking or any other of its business areas, by issuers or their subsidiaries, some of which could be analyzed in this report.

## Securities holdings and other disclosures.

As of the end of last quarter, Grupo Financiero Banorte S.A.B. of C.V. has not held investments, directly or indirectly, in securities or derivative financial instruments, whose underlying securities are the subject of recommendations, representing 1% or more of its investment portfolio of outstanding securities or 1% of the issuance or underlying of the securities issued.

None of the members of the Board of Grupo Financiero Banorte and Casa de Bolsa Banorte, along general managers and executives of an immediately below level, have any charges in the issuers that may be analyzed in this document.

The Analysts of Grupo Financiero Banorte S.A.B. of C.V. do not maintain direct investments or through an intermediary person, in the securities or derivative instruments object of this analysis report.

## Guide for investment recommendations.

Reference	
<b>BUY</b>	When the share expected performance is greater than the MEXBOL estimated performance.
<b>HOLD</b>	When the share expected performance is similar to the MEXBOL estimated performance.
<b>SELL</b>	When the share expected performance is lower than the MEXBOL estimated performance.

Even though this document offers a general criterion of investment, we urge readers to seek advice from their own Consultants or Financial Advisors, in order to consider whether any of the values mentioned in this report are in line with their investment goals, risk and financial position.

## Determination of Target Prices

For the calculation of estimated target prices for securities, analysts use a combination of methodologies generally accepted among financial analysts, including, but not limited to, multiples analysis, discounted cash flows, sum-of-the-parts or any other method that could be applicable in each specific case according to the current regulation. No guarantee can be given that the target prices calculated for the securities will be achieved by the analysts of Grupo Financiero Banorte S.A.B. C.V, since this depends on a large number of various endogenous and exogenous factors that affect the performance of the issuing company, the environment in which it performs, along with the influence of trends of the stock market, in which it is listed. Moreover, the investor must consider that the price of the securities or instruments can fluctuate against their interest and cause the partial and even total loss of the invested capital.

The information contained hereby has been obtained from sources that we consider to be reliable, but we make no representation as to its accuracy or completeness. The information, estimations and recommendations included in this document are valid as of the issue date, but are subject to modifications and changes without prior notice; Grupo Financiero Banorte S.A.B. of C.V. does not commit to communicate the changes and also to keep the content of this document updated. Grupo Financiero Banorte S.A.B. of C.V. takes no responsibility for any loss arising from the use of this report or its content. This document may not be photocopied, quoted, disclosed, used, or reproduced in whole or in part without prior written authorization from Grupo Financiero Banorte S.A.B. of C.V.

**GRUPO FINANCIERO BANORTE S.A.B. de C.V.**
**Research and Strategy**

Gabriel Casillas Olvera	Chief Economist and Head of Research	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godínez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967

**Economic Analysis**

Delia María Paredes Mier	Executive Director of Economic Analysis	delia.paredes@banorte.com	(55) 5268 - 1694
Katia Celina Goya Ostos	Senior, Global Economist	katia.goya@banorte.com	(55) 1670 - 1821
Juan Carlos Alderete Macal, CFA	Senior Economist, Mexico	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Miguel Alejandro Calvo Domínguez	Economist, Regional	miguel.calvo@banorte.com	(55) 1670 - 2220
Francisco José Flores Serrano	Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Luis Leopoldo López Salinas	Analyst, Global Economist	luis.lopez.salinas@banorte.com	(55) 1103 - 4000 x 2707
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611

**Fixed income and FX Strategy**

Alejandro Padilla Santana	Head Strategist – Fixed income and FX	alejandro.padilla@banorte.com	(55) 1103 - 4043
Santiago Leal Singer	FX Senior Strategist	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalía Orozco Vélez	Fixed Income and FX Strategist	leslie.orozco.velez@banorte.com	(55) 5268 - 1698

**Equity Strategy**

Manuel Jiménez Zaldivar	Director Equity Research — Telecommunications / Media	manuel.jimenez@banorte.com	(55) 5268 - 1671
Víctor Hugo Cortes Castro	Technical Analysis	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Equity Research – Conglomerates / Financials/ Mining / Petrochemicals	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Equity Research – Airlines / Airports / Cement / Infrastructure / REITs	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research – Auto Parts/ Consumer Discretionary / Real Estate / Retail	valentin.mendoza@banorte.com	(55) 1670 - 2250
Jorge Antonio Izquierdo Lobato	Analyst	jorge.izquierdo.lobato@banorte.com	(55) 1670 - 1746
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 – 4000 x 2755
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251

**Corporate Debt**

Tania Abdul Massih Jacobo	Director Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior, Corporate Debt	hugo.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Manager, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248

**Wholesale Banking**

Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(81) 8319 - 6895
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.cebaldos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Corporate Banking	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Víctor Antonio Roldan Ferrer	Head of Commercial Banking	victor.rolan.ferrer@banorte.com	(55) 5004 - 1454