

Banxico – We now forecast a 25pb hike in December

June 15, 2016

- We believe that today's FOMC statement, along with Chairman Yellen's speech drastically reduced the probability of a rate hike in the coming months
- In fact, our US economists now expect the FOMC to hike 25bps in December
- In this regard, we believe that Banxico will return to its more orthodox *modus operandi*, keeping monetary and FX policies separated
- Nevertheless, we acknowledge the risk of an additional rate hike, particularly in September, if the U.S. elections set off potential disorderly currency dynamics, which in turn could affect inflation expectations or financial stability
- We continue to believe that the central bank is still tied to the U.S. Fed actions, and Banxico's next move will be a 25bps rate hike in December, immediately after the Fed continues its normalization process

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The Fed will continue its hiking cycle in December. The monetary policy announcement released today by the FOMC, combined with the latest economic figures in the U.S. –particularly the last nonfarm payroll report–, drastically reduced the chances of a rate hike in the coming months. In this context, we consider that while other economic indicators point to an improvement in consumer spending, FOMC members do not want to cause additional market noise in the coming months. As a result, we now believe that the FOMC will resume its monetary normalizing process in December, with a 25bp rate hike.

Banxico will act in tandem with the Fed. Given Mexico's moderate economic growth, the absence of significant inflationary pressures, an expanded Flexible Credit Line -adding firepower to potential discretionary interventions if there are direct speculative attacks on the peso-, and the more dovish stance by the FOMC today, we believe that Banxico will return to its more orthodox *modus operandi*, keeping monetary and FX policies separated. In this regard, we believe that the central bank is still tied to the U.S. Fed actions, and Banxico's next move will be a rate hike, immediately after the Fed continues its normalization process in December 14. This implies that the central bank could be raising rates by 25bps in December 15. Nevertheless, we acknowledge the risk of an additional rate hike, particularly in September, if the US elections set off potential disorderly currency dynamics, which in turn could affect inflation expectations or financial stability.

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