

More dovish on growth... While acknowledging further downward revisions to global growth due to the pandemic, Banxico argued that activity contracted in 1Q20 and that the hit intensified in April, based on already published information. [Consistent with our view](#), they argued the reopening of some activities could help the recovery in May and June, albeit with the impact already high and with uncertainty persisting. We believe this signals a high likelihood that the central bank has already downgraded its [growth scenarios as presented in the latest QR](#), which estimated a mean contraction of 7.2% y/y in GDP for 2020. As a result, the monetary authority argued that “...*greater economic slack is expected within the time frame in which monetary policy operates...*”, resulting in a more negative output gap and with the balance of risks remaining significantly skewed to the downside even after recent adjustments to the outlook.

...while also skewing slightly towards lower inflation. Given the latter, they said that the downward impact on prices of a more negative output gap could be greater than previously expected. Moreover, they added lower inflationary pressures worldwide as a downside risk for inflation, replacing it for the effects of the decline in energy prices –with global crude oil prices increasing lately–. On the other hand, upside risks were basically left unchanged. Consequently, the statement included that “...*Regarding the foreseen trajectory for inflation, its determinants have slightly reduced it...*”. Nonetheless, the balance of risks is still characterized as uncertain. In our view, this is also related to additional challenges in assessing underlying price dynamics, with [higher volatility and surprises relative to market expectations](#), both mainly due to distortions related to the pandemic. Overall, it is our take that the central bank is more dovish at the margin regarding the outlook for inflation.

We now expect one more 50bps rate cut in September, with the reference rate at 4.00% by the end of year. Specifically, we now expect two additional 50bps rate cuts in the meetings to be held on August 13th and September 24th, with the reference rate ending the year at 4.00% (previous: 4.50%, with only one 50bps cut in August). Apart from today’s more dovish tone, additional monetary policy easing in both developed- and emerging-markets provides even more room for Banxico to continue easing policy. Importantly, this includes quantitative easing in countries such as India, Turkey, South Africa, Colombia and Chile. We believe the elimination of the comment, at the beginning of the document, that the central bank was ready to take necessary actions in a timely manner suggests a lower sense of urgency. Lastly, we recognize risks for financial stability stemming from the US election (November 3rd) remain in place, particularly for the September decision. Specifically, campaigns will already be in full force by that moment, with the most important event being the first Presidential Debate on September 29th. This is very relevant as it is our take that renewed bouts of volatility might emerge as: (1) President Trump could adopt a more aggressive stance towards Mexico; and (2) the rhetoric about trade, immigration or other controversial issues becomes more radical. Despite of the latter, we believe worldwide monetary policy conditions and the outlook for growth and inflation will continue supporting additional easing.

Banxico's 2020 policy decisions

Date	Decision
February 13	-25bps
March 20 (intra-meeting)	-50bps
April 21 (intra-meeting)	-50bps
May 14	-50bps
June 25	-50bps
August 13	--
September 24	--
November 12	--
December 17	--

Source: Banxico

From our fixed income and FX strategy team

We wait for better entry levels for long positions in long-term Mbonos with a fair valuation at the short-end of the local yield curve. Following Banxico's rate cut, the Mbonos curve experienced a partial profit taking of 3bps, holding daily gains close to 5bps that reached as much as 8bps in mid-term tenors. Meanwhile, TIEE-28 swaps strengthened their rally during the session with gains of 13bps in long-term securities, while the short-end rallied 5bps. This performance is consistent with our reading on Banxico's dovish tone and reflects a fair valuation at the shortest-end, reason why we hold our view of a more attractive relative value in long-term securities waiting for better entry levels in Mbonos. Considering the inflation risk balance presented by the central bank, it is worth highlighting the upward displacement registered in breakevens between Mbonos and Udibonos, that in all maturities have become more expensive since the last monetary policy decision. Particularly, 3- and 5-year tenors have elevated 75bps and 50bps since May 14th, to 3.06% and 3.11%, respectively.

In the FX market, the Mexican pesos' modest reaction reflected a widely priced-in decision, holding a performance highly related to global factors. In this sense, the peso closed the session with a 0.5% appreciation to 22.68 per dollar. In our view, the configuration of fragile optimism will remain affecting the currency's premiums which will also begin to adopt a stronger relation with geopolitical themes at the end of the 3Q20. In this context we see the USD/MXN 21.50 region as attractive for USD longs, stressing our caution view given the space of ample ranges and liquidity that has not recovered levels prior to the pandemic shock.

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