

Banxico Minutes – A divided Board regarding the room for a last cut

- Banxico published the minutes of the decision held on September 24th, in which the central bank cut the reference rate by 25bps to 4.25%, in a unanimous decision
- In our view, the tone of the minutes was less dovish, similar to the statement. In line with our expectations, the most important section was the debate about the ‘available room to maneuver’ for more cuts, in which we see divided opinions among Board members
- On growth, we identified few changes, recognizing some recovery in Mexico although with heterogeneous dynamics between external and domestic demand
- All members acknowledged recent short-term inflation pressures, with a renewed focus on risks to expectations despite still being convinced that it will converge to target in 2H21
- On financial stability, we highlight comments of better market conditions, with the majority adding risks of an unfavorable environment for private investment and to public finances after the release of the Budget Proposal for 2021
- We maintain our view that the reference rate will remain at 4.25% for the rest of the year and into 2021, despite possibly being a close call

Banxico minutes maintain a less dovish bias. Banco de México published the minutes of the meeting held on September 24th, in which the Board unanimously voted to cut the reference rate by 25bps to 4.25%. In our view, the tone of the minutes remains less dovish, similar to the last statement. Uncertainty over the next steps for monetary policy is still elevated, as portrayed by diverse comments by Board members. There were also relevant insights on inflation (particularly expectations) and financial stability risks, with opinions on growth broadly unchanged. Considering what we see as a divided Board, as well as a challenging short-term environment, we maintain our forecast of an unchanged reference rate at 4.25% for the remainder of 2020 and throughout 2021.

A divided Board on the ‘available room to maneuver’. It is our take that the most relevant section of the minutes was the discussion on this issue. Overall, we see a divided Board in this regard, with two members stating that this room still exists, two saying it does not, and one more uncertain. In our opinion, details in these minutes along other statements made in a series of forums are very helpful in judging how they stand in the dovish-hawkish spectrum (see chart below).

Banxico Hawk-o-meter



Source: Banorte; Images: Banxico Educa

October 8, 2020

www.banorte.com
@analisis_fundam

Gabriel Casillas
IRO and Chief Economist
gabriel.casillas@banorte.com

Alejandro Padilla
Executive Director of Economic Research
and Financial Markets Strategy
alejandropadilla@banorte.com

Juan Carlos Alderete, CFA
Director of Economic Research
juan.alderete.magal@banorte.com

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

Fixed income and FX Strategy

Manuel Jiménez
Director of Market Strategy
manuel.jimenez@banorte.com

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

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

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	-50bps
September 24	-25bps
November 12	--
December 17	--

Source: Banxico

Winners of the award for best economic forecasters for Mexico in 2019, given by *Refinitiv*



Document for distribution among the general public

From left to right, we believe Deputy Governor Gerardo Esquivel is the most dovish. In the minutes, we identify him with the statement that “...*the cycle of monetary easing should slow down, but that there is space to continue...*” and that it would not be convenient to send a signal that the cycle has ended. Among the reasons, he highlights a deeper economic contraction and lower one-year ahead inflation expectations relative to the 2009 financial crisis, that the credit channel operates in Mexico and lowering the rate could decrease borrowing costs, and the recent change of strategy by the Federal Reserve, among others.

On the other hand, it is our take that Deputy Governor Jonathan Heath considered that “...*monetary easing should continue given the depressed economic activity that faces a difficult, fragile and potentially long recovery...*”. He also thinks that the speed should be adjusted, focusing carefully on the performance of economic indicators in coming months –which stresses the need of being data dependent–. He then argues on four different factors: (1) The inflationary outlook, in which the current uptick in inflation may not be temporary; (2) that the absolute and relative monetary policy stance is starting to narrow; (3) that maintaining the current pace of easing could be interpreted as the price stability objective taking second stage; and (4) the importance of never disregarding inflationary concerns.

Third, Governor Diaz de León likely “...*highlighted monetary policy’s limited room for maneuver, and that in the future the available room will depend on the evolution of the factors that influence inflation forecasts...*”. He expanded on the challenges faced by monetary policy in a complex environment, including shocks to supply and demand and its effects on activity and inflation, along the fragility of global financial markets and risk appetite and risks of capital outflows, among others. In our view, these comments are very similar to those made in our podcast, [Norte Económico](#) (available only in Spanish), in which he participated as a special guest. We believe his comments give the strongest weight to the dependency on data and new information, which is inherently uncertain.

With a more hawkish bias, Deputy Governor Javier Guzmán is likely to have said that: “...*upward risks to inflation have increased...*” and that, coupled with other reasons, “...*this implies not only slowing down the pace of monetary easing, but also acknowledging that the margins of maneuver for additional easing have probably already exhausted, which underlines the convenience of beginning a pause after this decision...*”. Among them, he cites that inflation reached levels above the central bank’s expectations and target, the lower relative rate spread to emerging markets, inflation expectations not converging to target and other risks –such as the US presidential election, challenges for Pemex and public finances.

Lastly, we identified Deputy Governor Irene Espinosa as saying that “...*with the referred reduction of 25 basis points, the space for monetary policy has probably been exhausted...*” and that “...*the monetary policy announcement has to communicate that the trajectory and current levels of inflation have reduced the margin of maneuver for future rate cuts and that future decisions will depend on deviations that are observed in the trajectory of inflation to the 3% target...*”. She argued that prudence and caution should be reinforced when conducting monetary policy, highlighting high uncertainty (despite new and valuable information), the evolution of inflation expectations and idiosyncratic factors, among others.

Broadly unchanged views on growth. In our view, comments in this section had few significant changes. Among them, most members recognized that forecasts for the global economy this year have increased while those for 2021 declined. Regarding Mexico, the balance of risks remains skewed to the downside, with the majority expecting a difficult recovery subject to high uncertainty. In line with our view, they highlighted that the pickup in the economy in June and July has been heterogenous, driven by external demand –boosting manufacturing exports the most– while domestic demand has been weaker, reflected in consumption and investment and influenced by strong disruptions in the labor market. We believe these dynamics will prevail for longer, with the former mainly helped by strong stimulus measures in advanced economies, especially in the US.

Additional concerns on inflation, especially expectations. We obtained a bit more clarity on the possible skew on the balance of risks, which officially remains ‘uncertain’. Specifically, one member stated that “...*upward risks have increased...*”, while another mentioned that he/she considers it more balanced. ‘Some’ –referring to two members–, still consider it uncertain. More importantly in our view, members elaborated at length on expectations, especially given recent short-term inflation dynamics with everyone acknowledging its recent pick-up above 4%. Some members stated that expectations for 2020 and 2021 have continued to increase, with one specifying that “...*this suggests that the less favorable outlook has started to extend to the following year...*”. However, others maintain a more positive view, including one suggesting that mid-term and 2021 expectations have remained stable while those for the next 12 months have decreased. Despite of this, broad consensus remains that inflation will converge towards 3% in late 2021. Nevertheless, the pace seems to be more uncertain. Thus, we believe we might see a more careful approach ahead, consistent with the renewed focus on data dependency.

Macro financial risks continue to weigh on Board’s decisions. Despite recent improvements in financial markets –including operating conditions and some inflows into fixed-income assets–, one key factor stressed again is volatility, with comments from three members alluding to possible shocks due to external conditions. We believe this is especially significant considering the proximity of the US election as well as other sources of uncertainty. Domestically, they also elaborated on the outlook for investment on top of the usual concerns over public finances and Pemex. In the former, the majority judged that “...*there is an unfavorable environment for private investment...*”, with the broad message being a call of better conditions to foster growth, mainly targeting possible actions from the Federal Government. In public finances, some signaled that “...*several assumptions of the economic package might not materialize, emphasizing those related to the evolution of oil production and economic activity...*”. All in all, we consider that risks on these fronts support Banxico’s prudent and cautious approach.

We maintain our forecast of the reference rate remaining at 4.25%, despite possibly being a close call. This is mainly based on our view about the behavior of inflation (including its expectations) and financial markets in coming weeks and months. On prices, for the decision in November the latest available print will be October data, with our estimate still close to the 4% upper bound limiting additional cuts. On the other hand, and potentially more relevant, we see heightened volatility surrounding the US election, a factor also flagged as a risk by the Board. In our view, the possibility of not having a clear result on November 3rd would result in sharp market movements, not ruling out lower risk appetite and an impact in local assets. Although this effect would likely be temporary, specific conditions related to this election –including the pandemic, mail-in ballots, the relative spread in Electoral Votes–, could maintain volatility elevated for at least some weeks. On the contrary, if more favorable conditions materialize, we believe the deciding vote might ultimately rest on Governor Alejandro Díaz de León, given our assessment about Board members’ relative positions. In addition, we also reiterate our view of the reference rate remaining at 4.25% throughout 2021, with the possibility of additional cuts if more favorable conditions surrounding inflation and financial stability materialize in said year.

From our Fixed income and FX strategy team

We hold a view of steep slopes for the local yield curve going forward. The sharp steepening in the last sessions for the Mexican yield curve has come in line with our view of a short-end anchored with no further support from the expectation of greater monetary easing, and premiums related to the foreign backdrop adding to the performance at the long-end. In this sense, we see Banxico’s minutes as an element strengthening this reading, mainly when considering a market pricing in implied cuts for the reference rate by -8bps for 2020 and -13bps for the 2Q21, suggesting a very narrow range for variations at the short-end of the curve. Moreover, the local market reaction in the aftermath of the minutes has been consistent with this view. Following a positive price action at the beginning of the session with gains of ~4bps after CPI printed below expectations, rates have corrected with pressures that reach up to 1bp vs yesterday’s close at the long end, reflecting a market that acknowledges the limited space for Banxico’s maneuvers. The curve could take a temporal breather, although it is our take that it will hold a structure of steep slopes. In terms of strategy, we wait for better market conditions for directional recommendations given the elevated volatility in the following weeks ahead of the US electoral process and unsolved premiums linked to the pandemic.

In the FX market, the Mexican peso held a stable performance following the minutes trading between USD/MXN 21.40 and 21.50, extending gains for the second day and a positive weekly balance. After breaching the 200-day MA at 21.82 the MXN could hold a favorable momentum given the risk appetite scene and relative stabilization in the US dollar. We see next technical resistances at 21.30 and 21.10, watching for more attractive levels for USD longs, with grater conviction below 21.00.

Analyst Certification

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.

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
BUY	When the share expected performance is greater than the MEXBOL estimated performance.
HOLD	When the share expected performance is similar to the MEXBOL estimated performance.
SELL	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	IRO and Chief Economist	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godínez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
Economic Research and Financial Market Strategy			
Alejandro Padilla Santana	Executive Director of Economic Research and Financial Markets Strategy	alejandro.padilla@banorte.com	(55) 1103 - 4043
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251
Economic Research			
Juan Carlos Alderete Macal, CFA	Director of Economic Research	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Francisco José Flores Serrano	Senior Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Katia Celina Goya Ostos	Senior Economist, Global	katia.goya@banorte.com	(55) 1670 - 1821
Luis Leopoldo López Salinas	Economist, Global	luis.lopez.salinas@banorte.com	(55) 1103 - 4000 x 2707
Market Strategy			
Manuel Jiménez Zaldivar	Director of Market Strategy	manuel.jimenez@banorte.com	(55) 5268 - 1671
Fixed income and FX Strategy			
Santiago Leal Singer	Senior Strategist, Fixed Income and FX	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalía Orozco Vélez	Strategist, Fixed Income and FX	leslie.orozco.velez@banorte.com	(55) 5268 - 1698
Equity Strategy			
Marissa Garza Ostos	Director of Equity Strategy	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Senior Strategist, Equity	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Senior Strategist, Equity	valentin.mendoza@banorte.com	(55) 1670 - 2250
Victor Hugo Cortes Castro	Senior Strategist, Technical	victorh.cortes@banorte.com	(55) 1670 - 1800
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 - 4000 x 2755
Juan Barbier Arizmendi, CFA	Analyst	juan.barbier@banorte.com	(55) 1670 - 1746
Corporate Debt			
Tania Abdul Massih Jacobo	Director of Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior Analyst, Corporate Debt	hugoa.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248
Economic Studies			
Delia María Paredes Mier	Executive Director of Economic Studies	dela.paredes@banorte.com	(55) 5268 - 1694
Miguel Alejandro Calvo Domínguez	Senior Analyst, Economic Studies	miguel.calvo@banorte.com	(55) 1670 - 2220
Wholesale Banking			
Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(81) 8319 - 6895
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.cebillos@banorte.com	(55) 5268 - 9996
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Frigolet Vázquez Vela	Head of Sólida Banorte	alejandro.frigolet.vazquezvela@banorte.com	(55) 5268 - 1656
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Carlos Alberto Arciniega Navarro	Head of Treasury Services	carlos.arciniega@banorte.com	(81) 1103 - 4091
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
Lizza Velarde Torres	Executive Director of Wholesale Banking	lizza.velarde@banorte.com	(55) 4433 - 4676
Oswaldo Brondo Menchaca	Head of Specialized Banking Services	oswaldo.brondo@banorte.com	(55) 5004 - 1423
Raúl Alejandro Arauzo Romero	Head of Transactional Banking	alejandro.arauzo@banorte.com	(55) 5261 - 4910
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