

Banxico minutes – The tightening cycle will extend more months

- Banxico published the minutes of the decision held on February 9th, in which they hiked the interest rate by 50bps to 11.00%, with a unanimous vote. This was Deputy Governor Omar Mejía’s first meeting
- In our view, the document reaffirms the hawkish tone that we perceived in the statement, suggesting that concerns on inflation remain high
- We highlight the debate on actions ahead and guidance, noting:
 - (1) The dissenting opinion from Deputy Governor Espinosa, against signaling a possible reduction in the pace at the next meeting;
 - (2) Expectations that this moderation could materialize after the accumulated tightening achieved so far; and
 - (3) The perception that the forward guidance must be carried out cautiously due to potential data surprises
- Considering our view of a longer hiking cycle by the Fed and a more challenging inflation outlook, we now expect three 25bps hikes each in March, May, and June, with a terminal rate of 11.75% (previous: 11.50%). In addition, we no longer see cuts for the remainder of the year
- The market is betting on a 50bps hike in March, assigning a probability close to 72% to this scenario

Banxico’s minutes reaffirm a more hawkish tone. In our view, the document supports the reasons behind [the surprise hike in the corresponding policy decision](#). As such, the main factor driving the adjustment are concerns about the inflation outlook (particularly for the core), noting upward adjustments in the forecasts and the evolution of risks. In addition, there was an interesting debate about the guidance for the next meeting. Even though it is quite clear that another increase will materialize, there is some uncertainty regarding the magnitude. On the latter, we highlight the opinion from Deputy Governor Espinosa. Meanwhile, we saw several comments about the terminal level for the cycle and subsequent actions, although also with some uncertainty in this front. Finally, we must remember that this document had the first comments from Deputy Governor Mejía.

Inflationary pressures are still the main concern, classifying the outlook as complex and uncertain. The Board acknowledged that headline inflation has moderated, but that risks remain skewed to the upside. In addition, everyone considers as a matter of concern that the core has stayed high and with more persistence. While most noted that pressures are mainly from food items, there is also caution about the pickup in services early in the year. Moreover, they highlighted that part of the decrease in headline CPI has been supported by the non-core component (e.g. decreases in energy and agriculture). Finally, given the general upward adjustment in inflation forecasts along the horizon, the Board stressed that “... *the persistence of core inflation suggests that, looking ahead, its trajectory, albeit downward, will be above the previously anticipated one...*” Based on the latter, we believe that members will continue to assess inflation expectations the next decision, with a view on the terminal rate for the cycle and what it implies in terms of the ex-ante real rate.

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Banxico's 2023 policy decisions


Date	Decision
February 9th	+50bps
March 30 th	--
May 18 th	--
June 22 nd	--
August 10 th	--
September 28 th	--
November 9 th	--
December 14 th	--

Source: Banxico

Document for distribution among the general public

Additional adjustment in the next meeting. The statement was emphatic in mentioning that “...for its next policy meeting, the upward adjustment to the reference rate could be of lower magnitude...”, which in our opinion clearly signals that another hike is a sure thing. Nevertheless, the discussion on the magnitude was more interesting, with a divergence between members. The most hawkish remark was from Deputy Governor Espinosa, even adding a dissenting opinion on the statement, as seen in the table below. Meanwhile, we believe Deputy Governor Heath was more ambiguous, albeit still hawkish, mentioning that we are near the terminal point, but that the forward guidance might change. Also relevant, we found it hard to distinguish from Deputy Governor Borja and Deputy Governor Mejía –which we attribute to the time the latter spent as part of the former’s team. Nevertheless, we did distinguish some differences, with Mejía elaborating on the possibility of reducing the pace in March. Finally, Governor Rodríguez was the least hawkish, arguing that the pace of adjustment can be modified –which we think would be to the downside– and that we are very close to an adequate level to consolidate a downward path for CPI. In this context, we present some of the most relevant comments that we attribute to each member in the following table.

Banorte’s assessment on Board member’s comments in the February 9th minutes

Bias	Member	Order in the minutes	Relevant comments
 Hawkish	Irene Espinosa	2	<i>“...limiting the next decision by referring to a policy rate adjustment of lower magnitude implies a high and costly risk of correction if the assumptions do not materialize...”</i> <i>“...We must therefore be extremely cautious with our forward guidance. [...] without putting the central bank’s reputation at risk and without undermining the effectiveness of communication with markets...”</i> <i>“...given the possibility that inflation decreases faster in the United States than in Mexico, the road ahead for Banco de México would be longer...”</i>
	Jonathan Heath	3	<i>“... the forward guidance is data-dependent and that it does not represent an unwavering commitment...”</i> <i>“...it should be communicated that the central bank is currently close to reaching the terminal rate...”</i> <i>“...in order to maintain an ex-ante real interest rate above 6%, but without exceeding 7%...”</i>
	Omar Mejía	4	<i>“...the balance of risks for inflation will be compatible with a slower pace of adjustments in future monetary policy decisions...”</i> <i>“...a failure to act preemptively [...], there would be a synchronization of pressures which would imply relevant challenges for the behavior of core inflation...”</i> <i>“...decisions must remain flexible, dependent on incoming data...”</i>
	Galia Borja	1	<i>“...for the next decisions, it is necessary to take into account the tightening that has been achieved...”</i> <i>“...ongoing disinflationary process is especially uncertain given the atypical nature of the several inflationary shocks that have been faced...”</i> <i>“... the available information and its assessment should be key in every monetary policy decision...”</i>
	Victoria Rodríguez	5	<i>“...looking ahead, the pace of adjustments of the reference rate could be modified, and that it is very close to reaching a level that is appropriate to consolidate a disinflationary process in line with the inflation forecast...”</i> <i>“...for the next decisions, it is necessary to take into account the tightening that has been achieved and the fact that monetary policy operates with a lag...”</i> <i>“...an uncertain environment persists, despite the fact that certain pressures have been mitigated...”</i>
Dovish			

Source: Banorte with information from Banxico

Scattered comments on the terminal rate. Again, the most explicit insight was from Deputy Governor Heath, explaining the several stages of the tightening cycle. In this sense, we believe his most relevant point was that the ex-ante real rate should fluctuate somewhere between 6% and 7% –currently at 5.84%. Other comments were broader. Governor Rodríguez said that we could already be close to a final level, while Deputy Governor Espinosa argued that the road ahead could be longer than that of the Fed.

We anticipate three more 25bps hikes and a terminal rate of 11.75%. Based on these minutes and as we warned in the statement, we think the Board will keep discussing about the end of the cycle and the length that the rate will remain in restrictive territory. We believe most members see the terminal level close, albeit without further clarity on the magnitude of the following hikes and the period at which said level will be maintained. Hence, data dependence becomes more relevant. Along with upside risks on inflation and our call of further Fed tightening, we now estimate three more hikes of 25bps each in March, May, and June (previous: +25bps in March and May). As such, the rate would reach a terminal level of 11.75%, at which we expect to be kept at least until the end of this year (previous: 10.50%).

From our Fixed income and FX strategy team

The market is betting on a 50bps hike in March, assigning a probability close to 72% to this scenario. Local fixed-income securities backtracked some of the session's gains after Banxico's minutes. TIE swaps went from gaining 9bps to 7bps. Meanwhile, investors continue to debate the magnitude of the next rate hike from Banxico, with bets favoring the same pace as in the previous meetings (72% probability). Moreover, the market sees a higher terminal rate by August, close to 12.00%. In terms of strategy, we remain cautious and without directional positions due to increased uncertainty about the final level of the terminal rate in both the US and Mexico, as well as how long they will stay elevated. However, we recognize increased attractiveness in long-term Mbonos especially for long-term portfolios. In particular, the Nov'42, Nov'47, and Jul'53 maturities are undervalued relative to their duration-adjusted yield, trading around 9.40%. Furthermore, the MXN weakened from 18.35 to 18.45 per dollar, stabilizing later at 18.40 (-0.3%). The currency has maintained a defensive performance, supported by a more restrictive central bank stance. Among other factors, this has increased its appeal against EM peers, positioning itself as the strongest with a 6.0% price appreciation year-to-date.

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We, Alejandro Padilla Santana, Juan Carlos Alderete Macal, Alejandro Cervantes Llamas, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Katia Celina Goya Ostos, Francisco José Flores Serrano, José Luis García Casales, Víctor Hugo Cortes Castro, José Itzamna Espitia Hernández, Carlos Hernández García, Leslie Thalía Orozco Vélez, Hugo Armando Gómez Solís, Yazmín Selene Pérez Enríquez, Cintia Gisela Nava Roa, Miguel Alejandro Calvo Domínguez, Daniela Olea Suárez, José De Jesús Ramírez Martínez, Gerardo Daniel Valle Trujillo, Luis Leopoldo López Salinas, Isaías Rodríguez Sobrino, Paola Soto Leal, Daniel Sebastián Sosa Aguilar and Andrea Muñoz Sánchez, 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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