MNI Banxico Preview: September 2022

Executive Summary:

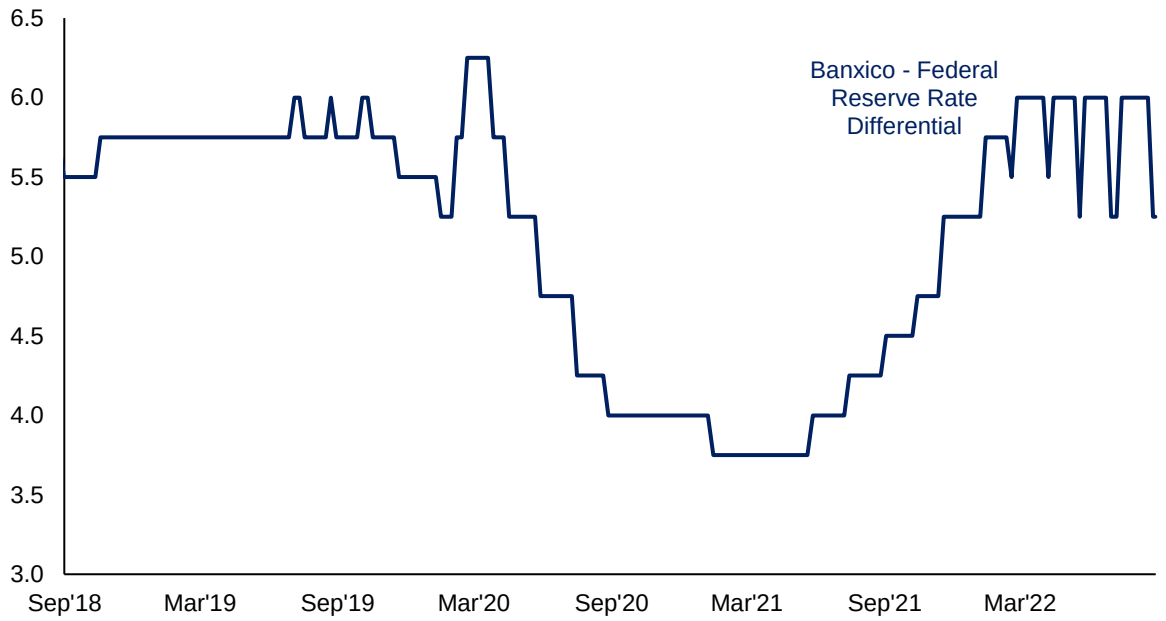
- **Banxico seen hiking rates by 75bps to reinstate policy differential with the Fed**
- **Evidence building of that bank could be nearing slower phase of tightening**
- **Focus will be on language, after August's statement opened the door to smaller rate hikes**

Rate Decision and Monetary Policy Statement: 1900BST / 1400ET, Thursday, September 29, 2022.

MNI Point of View: In lockstep with the Fed

Banxico are expected to raise rates by 75bps from 8.50% to 9.25% at the September meeting, keeping pace with the Fed's latest tightening step to match the US-Mexico rate differential back to 6 percentage points. Nonetheless, evidence is building that the Banxico could be nearing a slower phase for policy tightening, although the peak rate is still seen as some way off. Analysts are unanimous in forecasting a 75bps step from the Banxico this month, and a similar incremental change in August resulted in little market response.

Figure 1: Banxico likely to hike 75bps to reinstate the 6 ppts rate differential



Source: MNI/Bloomberg

Despite elements of a dovish turn in August's policy statement from the bank, still-high CPI and tightening conditions among trade partners should give the board ample justification for another 75bps step at this meeting. Markets will be on watch for any further tweaks in language after August's decision to remove the phrase "same forceful measures" from the statement. Instead, the MPC will likely retain the phrasing around future hikes being "based on the prevailing conditions" – a tweak that was read as dovish at the time.

Nonetheless, the over-arching tone of the statement remained hawkish, and the August CPI turn-out continues to support the balance of risks for inflation being "biased significantly to the upside". Both core and headline inflation tipped just ahead of market expectations, at 0.70% M/M and 0.80% for the core reading, suggesting plentiful pipeline inflation to keep the onus for rates pointed higher into year-end.

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Looking beyond this week's decision, analysts see further tightening of 150 – 250bps (including a presumed 75bps hike this week) before peak rates are reached – implying a terminal overnight rate at 10.00 – 11.00%. At this point, Banxico should have ample information with which to make a decision on whether to decouple from the Fed hiking cycle. With FOMC's Evans most recently suggesting that the Fed rate path could top out in March 2023, a pause to the Mexican tightening cycle in Q1 could garner favour among the board.

USDMXN started the week on a firmer note and traded higher Monday. Recent gains highlight the fact that the pair has failed to confirm a clear break of support at 19.8126, the Aug 15 low. Resistance at 20.2944, the Sep 1 high, has been breached. A clear break of this level would strengthen bullish conditions and open 20.8335, the Aug 3 high. On the downside, a break of 19.7533 would reinstate a bearish theme.

MNI Banxico Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
Bi-Weekly CPI	% y/y	8.76	7.7	↑	7.3	↑					1.56
Core CPI	% y/y	8.05	7.3	↑	6.6	↑					1.48
CPI	% m/m	0.70	0.2	↑	0.8	↓					0.10
Oil Price (WTI Active)	$	78.06	103.59	↓	83.11	↓					-0.33
Economic Activity		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
PMI Manufacturing	Index	48.5	50.6	↓	48.0	↑					0.43
GDP	% y/y	2.1	4.5	↓	-4.3	↑					0.05
Industrial Man Prod	% y/y	2.7	2.6	↑	4.3	↓					-0.60
Economic Activity IGAE	% y/y	1.27	1.35	↓	1.83	↓					-0.40
Monetary Analysis		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
M3 Money Supply	% y/y	10.3	9.4	↑	7.6	↑					0.55
Non-Fin Corp Credit	% y/y	-2.2	-0.3	↓	5.0	↓					-1.18
Household Credit	% y/y	16.4	16.5	↓	17.1	↓					-0.87
Consumer / Labour Market		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Retail Sales	% m/m	4.0	3.7	↑	5.2	↓					0.45
Consumer Confidence (Q)	Index	40.9	43.8	↓	43.5	↓					-1.74
Unemployment Rate	%	3.5	3.3	↑	3.7	↓					0.53
Nominal Wage Increase	% y/y	5.0	8.3	↓	7.0	↓					-1.28
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Bolsa Mexicana	Index	44,809	51,753	↓	53,401	↓					-1.56
10-Yr TIIE Swap Yield	%	9.41	8.48	↑	7.90	↑					0.76

Note: For quarterly data the 3m ago column will display the previous data point and the 6m ago column will display the data point prior to that.
Source: MNI, Bloomberg

Analyst Views (Alphabetical Order):

Bank of America: Expect Banxico to Hike in-line with Fed

- BofA believe Banxico will very likely keep hiking with the US Fed. Since their US economists now expect the Fed to hike to a 5% ceiling, they expect Banxico to hike to an 11% terminal rate (from 10% before).
- BofA change their Banxico call by adding more hikes and a higher terminal rate. They now expect Banxico to hike 75bp/75bp/50bp/25bp/25bp in Sept/Nov/Dec/Feb/March, respectively (the previous call was 75bp/50bp/25bp/0bp/0bp, respectively).
- Cuts are not expected of Banxico in 2023. In terms of risks, once the Fed is near the end of the cycle, Banxico may consider decoupling, but for now Banxico will likely move with the Fed and if core inflation remains surprising to the upside, it may even hike more aggressively than the Fed in the short term.
- Officials continue to put a lot of value on stability, prioritizing it over growth. At the Ministry of Finance, they are busy trying to keep the debt to GDP ratio in check and, at the central bank, they are busy trying to control inflation. Tight fiscal and monetary policies do not leave much room for growth.
- A vast majority at Banxico are worried about high inflation and especially about high core inflation and high inflation expectations. A vast majority as well seems to agree that there are external forces pushing inflation up. So, there is consensus that it is important to not let the peso depreciate, as otherwise this could amplify the impact of those external forces on inflation in Mexico.

- BofA believe that to fight inflation Banxico will try to prevent the peso from depreciating. This means that Banxico will try to maintain the current spread with the Fed, which many at the central bank think has worked well to reduce peso volatility.

Barclays: Expect 75bps Hike, 50bps Hike in December

- Barclays are of the view that Banxico is likely to maintain the spread at 600bp with respect to the FOMC target hiking 75bps on September 29. Furthermore, the domestic inflation outlook still requires a more restrictive stance.
- Mexico will probably be the last economy in Latin America to end its hiking cycle, as it has historically been the most tied to US monetary policy.
- The government is expected to announce further measures to fight inflation on October 3, but it is unclear if these will have an effect in the short term. What have really mattered are the fuel price subsidies. Annual inflation levels would be above 11% in the absence of these. All in all, these CPI numbers are in line with the view that Banxico will keep mirroring the Fed.
- Therefore, and according to the most recent forecasts from Barclays' US economics team, Banxico will likely hike 75bps next week and in November, then slow to 50bps in December, with a final hike of 25bps in February of next year, to reach a terminal rate of 10.75%.
- Barclays do not foresee any cuts in 2023, as inflation will likely remain above Banxico's target band.

Goldman Sachs: Expect 75bps Hike

- Given the recent domestic and external macro-financial developments, the policy signals and balance of views in the Aug 25 minutes and recent statements by several MPC members, Goldman expect the MPC to deliver another 75bps hike, driving the policy rate to 9.25%.
- Another 75bps rate hike is justified by the still-challenging current and prospective inflation outlook, further deterioration of short-, medium- and long-term inflation expectations, firm real GDP growth backdrop, improving labor market, and the FOMC 75bps hike and hawkish forward guidance on Sep 21.
- Goldman expect the forward guidance to remain data-dependent and the MPC to continue to express clear discomfort with the short-term inflation dynamics and to expect headline and core inflation to converge to the 3% target only by the end of the relevant horizon for monetary policy (1H2024)

JP Morgan: Expect 75bps Hike

- JPM expect Banxico to hike 75bps in line with the consensus, and contrary to their earlier expectations that changing gears to 50bps was reasonable in the context of Banxico's board signalling that they were ready to adopt a more flexible approach in the current hiking cycle.
- JPM now expect inflation, both headline and core, to average 8.5% in 4Q22. They see inflation near 6%
- Upward surprises to inflation in the US and the hawkish pivot from the Fed this week suggests Banxico will have to stay a little longer at 75bps before returning to 50bps in 4Q. JPM now expect Banxico to end its hiking cycle at 10.25% by the end of 3Q23.

Scotiabank: Expect 75bps Hike, Though Note Slight Less-Hawkish Change in Statement Tone

- Considering the Fed's latest 75bps hike and local headline inflation coming in higher than consensus (with the core component rising), Scotiabank have no doubt that Banxico will raise its policy rate by 75bps for the third consecutive time, to 9.25%, matching the Fed's pace of tightening.
- Though the tone of the statement was virtually unchanged, the Fed's outlook now has a more restrictive sense, even suggesting a terminal rate near 5%, which could mean an additional 75bps and a further 50bps increase later this year.
- They expect Banxico to update its outlook in next week's communiqué, showing a higher inflation peak than its previous forecast, keeping it at elevated levels for a longer period, and only approaching the 3% target after Q1-2024, in line with the Fed's new expected inflation trajectory.

- Regardless of these factors, Scotiabank do not expect the decision for a 75bps increase to be unanimous. One reason for this is that at the August meeting the Board removed the word “forceful” from the statement regarding the measures to be taken as conditions require.

SocGen: Expect 75bps Hike, Followed by Two 50bps Hikes

- SocGen expect Banxico to implement another 75bps rate hike in September. SocGen recently revised up their year-end and terminal Banxico rate forecast from 9.25% to 10.25%. Nevertheless, in light of a hawkish Fed statement this week, they see considerable upside risks to both their year-end and terminal Banxico rate forecasts.
- Although Banxico still expects inflation to converge to the target during the policy horizon, SocGen see core inflation staying above it throughout. The risks to their near-term inflation forecast are skewed to the upside given the inherent inertia amid a tight labour market.
- SocGen’s current Banxico rate forecasts are for a 75bps hike in September to be followed by 50bps hikes in each of the two meetings in 4Q22, taking the overnight rate to 10.25% this year (also the terminal rate forecast).
- Apart from the high and rising inflation, the Bank of Mexico’s rate decision equally reflects its policy alignment with the Fed.
- SocGen also see a significant possibility (about 30% probability) of a 100bps Banxico rate hike in September. In any case, until the core inflation begins to subside, it would be premature for the market to expect the end of the tightening cycle.

TD Securities: Expect 75bps Hike in-line with Fed

- TD expect Banxico to hike rates by 75bps. While they had previously expected 50bps, they now think the Bank will continue to go in tandem with the Fed. This also means a 75bps hike in Nov and 50bps in Dec.
- Whether Banxico can start decoupling next year is a matter that depends on the CPI (still at 8.7% y/y in Aug) and MXN performance, which TD will reassess in the near future.

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