

May 14, 2020

## Press Release

**Monetary Policy Statement**

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**Banco de México's Governing Board decided to lower the target for the overnight interbank interest rate by 50 basis points to 5.5%.**

In view of the complex economic and financial situation worldwide, Banco de México has been closely monitoring the behavior of domestic financial markets, economic activity and inflation, in order to take the necessary actions in a timely manner. The COVID-19 pandemic and the measures adopted to prevent its spread have affected world economic activity considerably. This has led to unprecedented revisions of economic expectations, which incorporate a strong contraction of productive activity in 2020. In turn, this has resulted in a sharp fall in commodity prices, especially of crude oil. As a consequence of these factors, several central banks have reduced interest rates significantly and implemented other extraordinary measures to foster the proper functioning of their financial markets. Likewise, several countries have implemented fiscal stimulus measures to mitigate the adverse effects on employment and on households and firms' income.

This environment has led to a significant deterioration of global financial conditions, to a recomposition of investors' portfolio towards lower risk assets, and to the greatest contraction ever recorded of holdings of emerging economies' assets, especially of fixed-income instruments. This adjustment contributed to a depreciation of these economies' currencies and to volatility in their foreign exchange markets, including the Mexican peso. The actions adopted by advanced economies to provide liquidity and restore financing have contributed to the more stable behavior observed in international financial markets. Such actions have also contributed to the better performance of domestic financial markets over the last weeks, where lower interest rates on government securities for all terms were registered, while the Mexican peso exchange rate traded in a narrower range. Nevertheless, global and domestic financial conditions will continue to be subject to the outlook for the effects of the pandemic.

Available information shows that economic activity in Mexico contracted significantly during the first quarter of the year, incorporating the effects associated with the pandemic in March, which affected the production of goods and services considerably. Although the magnitude and duration of the effects of the pandemic are still unknown, these are expected to intensify during the second quarter, and to result in a significant contraction of employment. Slack conditions thus continue to widen considerably, in a context in which the balance of risks for growth is significantly biased to the downside.

Annual headline inflation decreased from 3.25 to 2.15% between March and April 2020 due to declines from 2.19 to -1.96% and from 3.60 to 3.50% in its non-core and core components, respectively. A particularly relevant factor was the decline in the annual change of energy prices, particularly of gasoline. Short-term expectations for headline inflation have decreased, while those for long and medium terms have remained relatively stable, albeit at levels above the 3% target.

The challenges for monetary policy posed by the pandemic include both the unprecedented impact on economic activity as well as those associated with the financial shock that we are currently facing. As for the risks to the foreseen trajectory of inflation, the most important to the downside are a significant widening of the negative output gap and the effects of the fall in energy prices. To the upside, a greater or more persistent depreciation of the peso and possible disruptions to chains of production and distribution of certain goods and services. In this context, the balance of risks for inflation remains uncertain.

Taking into account the referred risks for inflation, economic activity and financial markets, major challenges arise for monetary policy and for the economy in general. Considering the room for maneuvering that on balance monetary policy has as a result of these implications, and with the presence of all its members, Banco de México's Governing Board decided unanimously to lower the target for the overnight interbank interest rate by 50 basis points to a level of 5.5%.

The Governing Board will take the necessary actions on the basis of incoming information and considering the large impact on productive activity as well as the evolution of the financial shock that we are currently facing, so that the policy rate is consistent with the orderly and sustained convergence of headline inflation to Banco de México's target within the time frame in which monetary policy operates. Perseverance in strengthening the macroeconomic fundamentals and adopting the necessary actions, regarding both monetary and fiscal policies, will contribute to a better adjustment of domestic financial markets and of the economy as a whole.