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Press Release

Monetary Policy Statement

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Banco de México's Governing Board has decided to maintain the target for the overnight interbank interest rate at 8.25%.

Available indicators suggest that the weakening of world economic activity observed during the second half of 2018 continued during the early part of 2019, as evidenced by the lower dynamism in most advanced and some emerging economies, such as the euro area, China, and, to a lesser extent, the United States. This has led to a decline in global growth expectations. Labor markets in the major advanced economies continued exhibiting tightness. Nevertheless, headline inflation in these economies has decreased, partly due to the lower energy prices in relation to the previous year, while core inflation has remained relatively stable. All of the above has consolidated expectations that the major central banks would not tighten monetary conditions in the foreseeable future. In March, the Federal Reserve left the target range for the federal funds rate unchanged and reiterated its message that it will be patient in making future adjustments to the target range. In addition, the median of the Federal Open Market Committee (FOMC) economic projections suggests that there will be no increases in the federal funds target range in 2019. The Fed also announced significant changes in the strategy for the normalization of its balance sheet, which consists of shrinking the rate of reduction of its securities holdings starting in May and concluding such process in September of this year. In this context, the interest rates of U.S. Treasury bonds decreased significantly for all terms, thus increasing risk appetite in financial markets and leading to higher capital flows to emerging economies. In this regard, it is important to highlight that risks to the global economy persist, among which a sharper deceleration than previously foreseen, the uncertainty regarding trade disputes between the U.S. and China, a disorderly Brexit process, a lower-than-expected growth of the Chinese economy, and an escalation of political and geopolitical turmoil in different regions, stand out.

Since the last monetary policy decision, the more favorable conditions that have prevailed in international financial markets have contributed to the positive performance of financial assets in Mexico. Nevertheless, some risk factors and the uncertainty associated with the Mexican economy have led to an additional discount or risk premium for domestic assets. Among such factors, those related to the credit rating of Pemex, and even to Mexico's sovereign debt, are particularly noteworthy.

The current environment continues to pose significant risks in the medium and long terms that could affect the country's macroeconomic conditions, its potential growth, and the economy's price formation process. In this regard, it is particularly important that, in addition to following a prudent and firm monetary policy, measures to foster an environment of confidence and certainty for investment and higher productivity are adopted, and public finances are consolidated sustainably. In this context, it is especially relevant that the fiscal goals set in the Economic Package for 2019 are attained. Strengthening the rule of law and tackling corruption are equally imperative.

Available information suggests that, in the early part of 2019, Mexico's economy continued registering low growth as a result of the slowdown of the world economy, some weakness in domestic demand, and transitory factors that might have affected growth during the first quarter of the year. Thus, slack conditions in the economy loosened towards the end of 2018 and the early part of 2019. Due to the latter, the balance of risks for growth remains biased to the downside.

Between January and the first two weeks of March, headline inflation fell from 4.37% to 3.95%, mainly due to the decline in non-core inflation, which went from 6.81% in January to 5.39% in the first two weeks of March, as a result of the lower increases in energy and in agricultural and livestock product prices. Nevertheless, some of the favorable shocks that have led to the fall in non-core inflation have started to revert recently. In particular, the prices of energy goods rose in the second half of February, reflecting increases in their international references. With regards to core inflation, it evolved as anticipated, by registering 3.60% in January and 3.51% in the first two weeks of March. Nevertheless, food merchandise inflation has increased, while that of certain services remains high. As for inflation expectations, between January and February the median of headline inflation expectations for 2019 and 2020 fell from 3.80% to 3.65%, and from 3.71% to 3.60%, respectively. However, that of core inflation expectations for the end of 2019 remained at 3.50%, while that for the end of 2020 increased slightly from 3.45% to 3.48%, during the stated period. As for headline inflation expectations for the medium and long terms, these continue to be above the 3% permanent target, at around 3.50%. Regarding medium-term core inflation expectations, these increased from 3.42% to 3.50%, while those for the long term remained at 3.40%, after having been at 3.30% during most of 2018. As for information drawn from market instruments, the medium- and long-term inflationary risk premium decreased, although it still remains at high levels.

As for inflation risks, the possibility that the peso exchange rate comes under pressure stemming from external or domestic factors stands out. Should the economy require adjustments either to the real exchange rate or to medium- and long-term interest rates, Banco de México will contribute to making such adjustments occur in an orderly manner, in an effort to prevent second-round effects on the economy's price formation process. Inflation could also be affected if additional pressures on energy prices or on agricultural product prices arise, if an escalation of protectionist and compensatory measures worldwide materializes or in case public finances deteriorate. Considering the magnitude of the minimum wage increases, in addition to their possible direct impact, there is also the risk that these bring about wage revisions that exceed productivity gains and give rise to cost pressures, affecting formal employment and prices. In order to raise the purchasing power of wages sustainably, the role of other public policies must be considered, in particular, fostering competition in those sectors of goods and services with a high share in the consumption basket of the segments of the population with the lowest income. Also, the persistence shown by core inflation could give rise to a greater resistance to decline of long-term inflation expectations. As for downside risks, those that stand out are possible lower price increases in some of the goods included in the non-core subindex or a greater-than-foreseen widening in slackness conditions. Altogether, although there has been an intensification of some of the downside risk factors, there are still others that might put upward pressure on inflation in greater magnitude and make it deviate from its foreseen path. For this reason, the balance of risks for the forecasted trajectory for inflation still remains to the upside, in an environment of high uncertainty.

To guide its monetary policy actions, Banco de México's Governing Board follows closely the development of inflation vis-à-vis its forecasted trajectory, taking into account the monetary policy stance and the time frame in which monetary policy operates, as well as available information on all inflation determinants and on medium- and long-term inflation expectations, including the balance of risks for such factors. Monetary policy must respond prudently if for any reason the uncertainty faced by the economy increases considerably. In this context, considering that the recent developments in inflation and its main determinants have not changed significantly with respect to their foreseen path, that the cyclical position of the economy has loosened somewhat, and that the current monetary policy stance is consistent with

the convergence of inflation to its target, Banco de México's Governing Board has decided unanimously to leave the target for the overnight interbank interest rate unchanged at 8.25%. Considering the risks to consolidate low and stable inflation as well as those the economy's price formation is subject to, the Governing Board will take the necessary actions so that the reference rate is kept at a level consistent with the convergence of headline inflation to Banco de México's target within the time frame in which monetary policy operates.

Banco de México's Governing Board will maintain a prudent monetary policy stance and, under the current environment of uncertainty, will follow closely the potential pass-through of exchange rate fluctuations to prices, Mexico's monetary policy stance relative to that of the U.S.-in an external environment that it is still subject to risks- and the behavior of slack conditions in the Mexican economy. In the presence and possible persistence of factors that, by their nature, involve risks to both inflation and inflation expectations, monetary policy will be adjusted in a timely and firm manner to achieve the convergence of inflation to its 3% target and to strengthen the anchoring of medium- and long-term inflation expectations so that they attain such target.