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Mexico—Banxico Pauses Rate-Cut Cycle with No Surprises

- **Banxico's Governing Board kept the policy rate unchanged at 7.00%, in line with consensus expectations, in a unanimous vote.**
- **Headline and core inflation forecasts were revised upward, with convergence to the 3% target now expected in Q2 2027.**
- **The tone of the statement showed a significant shift compared with previous meetings, halting the easing cycle after eleven consecutive rate cuts.**
- **We maintain our year-end policy rate forecast at 6.50%, subject to the trajectory of inflation, the exchange rate, and the Mexico–U.S. rate differential.**

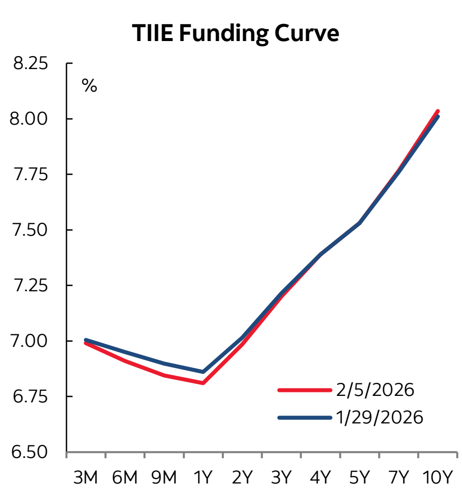
Banco de México's Governing Board unanimously decided to keep the policy rate unchanged at 7.00%, in line with expectations, pausing the easing cycle after eleven consecutive meetings with cuts: four cuts of 25 basis points in 2024, plus three 25 bp cuts and four 50 bp cuts during 2025. Notably, the Board revised upwards its forecasts for both headline and core inflation and pushed back the expected convergence to the 3.0% inflation target from Q3 2026 to Q2 2027.

The statement stated that during Q4 2025 global economic activity continued to moderate amid persistent trade tensions, while in major advanced economies headline inflation showed a slight decline and core inflation remained somewhat persistent. It highlighted that the Federal Reserve kept its policy rate unchanged in January, and financial markets performed positively though with volatility, with limited movements in U.S. Treasury yields and a depreciation of the dollar. Key global risks include a possible escalation of trade tensions and worsening geopolitical conflicts, which could affect inflation, growth, and financial stability.

At home, the Board noted that since the last policy meeting, yields on Mexican government securities declined across all maturities, while the USDMXN appreciated. In Q4 2025, economic activity recovered after the contraction in the previous quarter. However, uncertainty and trade tensions continue to pose downside risks to growth.

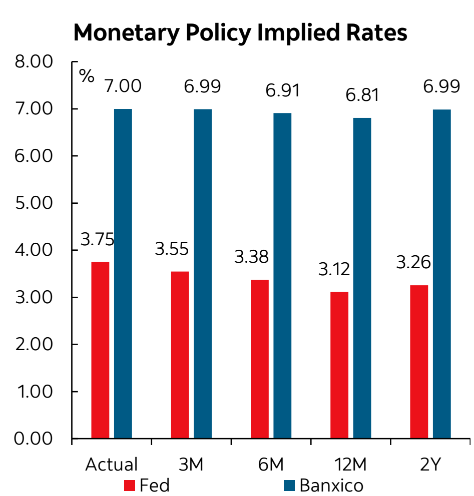
Regarding inflation, the Board stated that between November 2025 and the first half of January 2026, headline inflation edged down slightly from 3.80% to 3.77% y/y, owing to a decrease in the non-core component, while core inflation increased from 4.43% to 4.47% y/y. They also noted that market expectations for year-end 2026 inflation rose, and although longer-term expectations remained stable, they remain above target.

Chart 1



Sources: Scotiabank Economics, Bloomberg.

Chart 2



Sources: Scotiabank Economics, Bloomberg.

Accordingly, Banxico revised its headline and core inflation forecasts upward for 2026 and early 2027 due to a higher projected path for core inflation. Inflation is now expected to converge to the 3% target in Q2 2027, rather than in Q3 2026 as previously anticipated. These forecasts remain subject to both upside risks—including persistent inflation, cost pressures, peso depreciation, geopolitical disruptions, and climate-related shocks—and downside risks, such as weaker economic activity, lower cost pass-through, or a stronger USDMXN. However, the balance of risks remains biased to the upside, while uncertainty surrounding U.S. economic policy changes continues to influence the outlook.

We consider the policy decision reflects a less dovish stance in comparison to previous meetings, given both the pause and the unanimous vote. The revision to the projected date of inflation convergence from Q3 2026 to Q2 2027, as well as the upward adjustment in expectations, is consistent with the decision.

However, the statement keeps the door open for additional rate cuts, noting that “looking ahead, the Board will evaluate additional reference rate adjustments. It will consider the effects of all determinants of inflation.” Therefore, it will be essential to monitor inflationary risks, domestic economic weakness, the exchange rate, labour-market conditions, and U.S. inflation. These factors could strongly influence Banxico’s next decision.

In this context, we believe that the likelihood of Banxico continuing with the easing cycle in the March decision has decreased. We maintain our expectation of a 6.50% policy rate at the end of 2026, assuming no second-round effects from higher excise taxes, tariffs, and minimum -wage increases; a relatively stable USDMXN; and that the Mexico–U.S. interest rate spread does not fall below 325 basis points. Finally, the minutes of this decision—scheduled for release on February 19th, 2026—will be particularly important to get on details each board member's stance.

Regarding the market reaction, USDMXN showed virtually no response to the decision and remained at 17.39 pesos per dollar. The TIIE curve showed mixed movements: the one-month tenor rose 20 basis points, while maturities up to one year fell about 3 bps, and the rest of the curve declined between 7 and 8 bps. The three-month implied curve stood at 6.99%, and the one-year at 6.81%. Analysts surveyed expect the policy rate to close 2026 at 6.50%, with responses ranging from 6.00% to 7.00%.

Table 1: Banxico's Headline and Core Inflation Forecasts (%)

Headline Inflation	**25-Q3**	**25-Q4**	**26-Q1**	**26-Q2**	**26-Q3**	**26-Q4**	**27-Q1**	**27-Q2**	**27-Q3**	**27-Q4**
Current (Feb. 26) e.o.p.	3.6	3.7	4.0	3.8	3.6	3.5	3.2	3.0	3.0	3.0
Previous (Dec. 25) e.o.p.	3.6	3.7	3.7	3.3	3.0	3.0	3.0	3.0	3.0	3.0
Var. Current - Previous	0.0	0.0	0.3	0.5	0.6	0.5	0.2	0.0	0.0	0.0
Core Inflation	**25-Q3**	**25-Q4**	**26-Q1**	**26-Q2**	**26-Q3**	**26-Q4**	**27-Q1**	**27-Q2**	**27-Q3**	**27-Q4**
Current (Feb. 26) e.o.p.	4.2	4.3	4.4	4.0	3.6	3.4	3.1	3.0	3.0	3.0
Previous (Dec. 25) e.o.p.	4.2	4.3	4.0	3.4	3.0	3.0	3.0	3.0	3.0	3.0
Var. Current - Previous	0.0	0.0	0.4	0.6	0.6	0.4	0.1	0.0	0.0	0.0

Sources: Scotiabank Economics, Banxico.