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Mexico—Banxico Delivered the 75bps Expected Hike

- Some fracturing of views in the governing board observed.

Banxico hiked its policy rate by 75bps, as widely expected, to 10.00%, summing. This is the fourth consecutive increase of this size. This was not a unanimous decision as Deputy Governor Gerardo Esquivel voted for a 50bps hike. The forward guidance remained largely unchanged from the previous decision, with Banxico's communiqué stressing that it will evaluate "the prevailing conditions" in its upcoming decisions, although the statement mentioned that the board also considered "the monetary stance already attained in its hiking cycle". Additionally, inflation forecasts did not change notably on this occasion; in fact, inflation expectation for Q4-2022 marginally diminished (table 1), while the expectation of convergence to the 3.0% target remained unchanged at Q3-2024. Despite this, the governing board considered that, although some shocks show signs of subsiding, the balance of risks in the inflation trajectory remains biased to the upside.

The statement highlighted the decline in headline inflation in October, which stood at 8.41%, although it mentioned that the fall was led by the non-core component, as core inflation continued its upward trajectory, standing at 8.42%. Thus, Banxico negatively revised its short-term headline inflation expectation to 8.5% on average in Q4-2022. It maintained the 3.1% expectation for Q3-2024. In contrast, the expected trajectory of core inflation rose modestly from 2023 onwards, again expecting it to reach 3.0% in Q3-2024.

As headline inflation appears to have started a downward trend, the dynamic of core inflation suggests that it is not yet a good time to decouple from the Fed's hikes. The least volatile component of inflation and in many ways the most important for monetary policy, core inflation, continued to accelerate in October, albeit less than anticipated. In addition, the statement highlights an upward skew to the balance of risks. Thus, although at least one of its members considers that it is time to differentiate from the Fed's pace of hikes, we do not believe that there are sufficient conditions to do so. In this regard, it is worth mentioning that, although this could be Deputy Governor Esquivel's second-to-last meeting, the member who takes his place could also have a dovish bias. **Therefore, we believe that Banxico will follow the Fed's December decision with a 50-point hike, to end the year at 10.50%.**

For now, we stick to an outlook of an additional hike in early 2023, leaving the stance unchanged for most of the year. A cut is expected in Q4-2023. Thus, we maintain our end-2023 rate forecast at 10.50%, but with downside risks of a possible decoupling of the Fed's stance sooner than anticipated.

Table 1: Mexico—Banxico's Headline and Core Inflation Forecasts

Headline (y/y % change)	22Q1	22Q2	22Q3	22Q4	23Q1	23Q2	23Q3	23Q4	24Q1	24Q2	24Q3
Nov. '22 (eop)	7.3	7.8	8.5	8.3	7.6	5.8	4.7	4.1	3.8	3.4	3.1
Sep. '22 (eop)	7.3	7.8	8.6	8.6	7.9	6.0	4.8	4.0	3.7	3.4	3.1
Change	0.0	0.0	-0.1	-0.3	-0.3	-0.2	-0.1	0.1	0.1	0.0	0.0
Core (y/y % change)	22Q1	22Q2	22Q3	22Q4	23Q1	23Q2	23Q3	23Q4	24Q1	24Q2	24Q3
Nov. '22 (eop)	6.5	7.3	8.0	8.3	7.5	6.4	5.2	4.1	3.6	3.2	3.0
Sep. '22 (eop)	6.5	7.3	8.0	8.2	7.3	6.2	5.0	4.1	3.6	3.2	3.0
Change	0.0	0.0	0.0	0.1	0.2	0.2	0.2	0.0	0.0	0.0	0.0

Sources: Scotiabank Economics, Banxico.

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