

Banxico Watch

Banxico turns less hawkish...

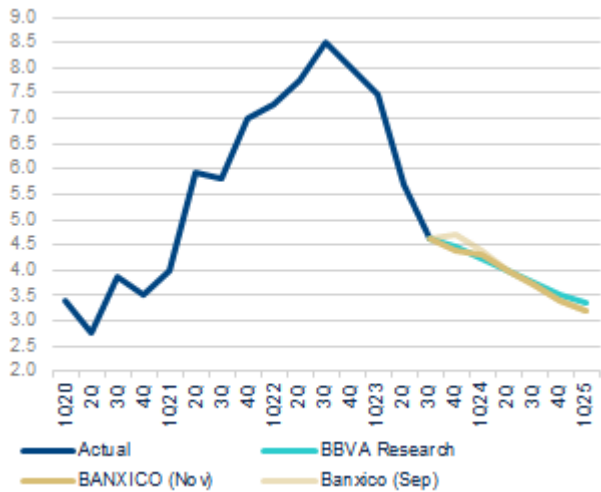
Javier Amador / Iván Fernández / Carlos Serrano
November 9, 2023

... and paves the way to start a rate cut cycle in early 2024

- **Banxico kept the policy rate unchanged at 11.25% for the fifth consecutive meeting and revised down its short-term headline inflation forecasts.** Back in September, Banxico puzzlingly revised up its short-term headline inflation forecasts to 4.7% and 4.4% YoY for 4Q23 and 1Q24. As we argued yesterday ([see](#)), with October's headline inflation set to fall to levels slightly below 4.3%, Banxico was likely to revise down these forecasts, bringing its path closer to ours again ([Figure 1](#)). That is, September's expectation that headline inflation was set to decline more gradually than previously foreseen, Banxico now expects it "will remain on a downward trend." With core inflation easing in line with its previous forecasts, the path was left unchanged. In line with our view, Banxico continues to think that core inflation will keep steadily easing.
- **More importantly, there was a significant shift of tone in the statement that suggests that discussions to avoid a more restrictive stance in the coming months have started.** Although it remained hawkish, there were several tweaks to the statement that shifted its tone to less hawkish. Banxico acknowledged that year-end core inflation expectations have recently come down (moving closer to our forecast), and even though in Banxico's view the balance of risks for inflation remains biased to the upside, the outlook that was recently deemed as "very complex" is now viewed as "challenging." **The most noteworthy change in the wording came in the forward guidance paragraph.** After signaling in September that the policy rate was set to remain unchanged "for an extended period," Banxico now says that it must be kept unchanged "for some time."
- **In a nutshell, Banxico paved the way to start a rate cut cycle in 1Q24 if inflation continues to ease as expected.** Considering that the recent rhetoric from Banxico and some members of the Board had recently turned more hawkish alongside the puzzling upward revision of its short-term inflation forecasts in September, today's shift of tone was surprising, as evidenced by the USDMXN going up by c. 30 cents following the statement release. Not because it was not warranted, but because there were no signs that it could have happened today. We had been arguing for some time that a rate cut cycle would be warranted sooner rather than later to avoid a further tightening of the monetary policy stance with falling inflation and the real rate set to rise further. Even if an easing cycle starts in 1Q24 as we continue to expect, the monetary policy stance would not become less restrictive. With expectations that inflation would come down to levels closer to the upper limit of the variability range by 1Q24, it seemed warranted. **Today's changes to the statement suggest that members thought it was appropriate to convey now that a start of a rate cut cycle in 1Q24 was becoming increasingly likely.** We continue to expect rate cuts to start in early 2024, and after today's significant shift of tone of the forward guidance, **we no longer think that we need to push back further the timing of the start of the rate cut cycle**, but at the same time, we now think that Banxico's first moves could be more gradual. Thus, **we continue to think that Banxico will end up bringing down the monetary policy rate to levels closer to our current below-consensus forecast (of 8.25%) by the end of next year, but we have an upward bias.**

Banxico's short-term expected inflation path now mirrors ours, as we anticipated; core inflation...

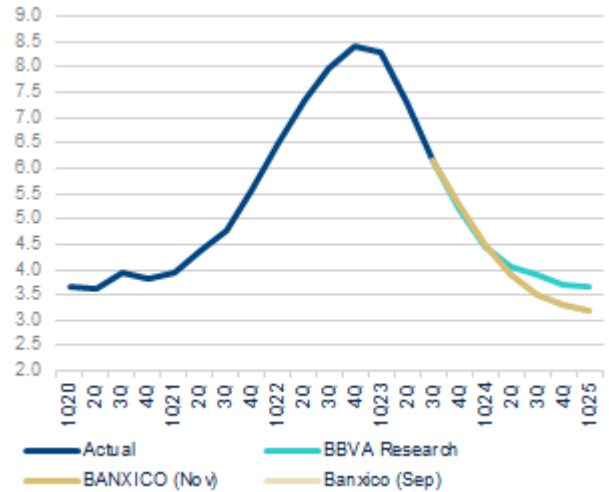
Figure 1. **HEADLINE INFLATION OUTLOOK**
(YOY % CHANGE, QUARTERLY AVERAGE)



Source: BBVA Research based on data by Banxico and INEGI.

... forecasts were left unchanged as Banxico continues to think it is set to steadily ease

Figure 2. **CORE INFLATION OUTLOOK**
(YOY % CHANGE, QUARTERLY AVERAGE)



Source: BBVA Research based on data by Banxico and INEGI.

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