Banxico Watch

Banxico refrains from hinting a rate cut in February…

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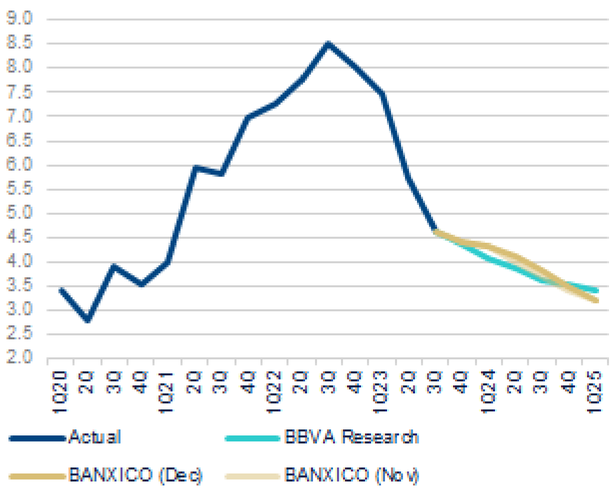
December 14, 2023

… and continues to signal that it is unlikely to cut rates at consecutive meetings at the start of the rate-cutting cycle

- **Banxico kept the policy rate unchanged at 11.25% for the sixth consecutive meeting and fine-tuned its headline and core inflation forecasts somewhat to the upside**, which now "incorporate a more gradual decline in both food merchandise inflation and services inflation." Headline inflation was marginally revised up by 0.1 pp for the last three quarters of 2024, to 4.1, 3.8, and 3.5%, respectively, while core inflation is now expected to decline more gradually to 3.5% (3.3% previously) by 4Q24. Thus, Banxico brought its 2024 core inflation expected path closer to ours (Figure 2).
- **The statement retained the more moderate hawkish tone from the November's meeting, as the Board continued to signal that the policy rate "must be maintained at its current level for some time."** We expected this to be the case (see) and, in our opinion, today's decision and messages did not definitively close the doors to a rate cut in the first meeting of next year. While Board members continued to characterize inflationary risks as biased to the upside, a dovish tweak in the statement showed that they also recognized that the ongoing "disinflation process is expected to continue, in view of the monetary stance and the easing of the shocks generated by the pandemic and the war in Ukraine." It is true that the Fed's surprising dovish shift this week could have been a good reason for Banxico to feel more confident in signaling more clearly the growing chances of a rate cut in February next year. However, it seems that the consensus among Board members was to opt for a more cautious strategy given a "challenging" outlook that still appears complex and uncertain due to the idiosyncratic nature of inflationary pressures, particularly on services inflation. In any case, the unchanged tone of the statement seems to confirm that the beginning of the rate cut cycle will be gradual, i.e., it seems likely that the first two rate cuts will not occur in consecutive meetings because, as Deputy Governor Heath has extensively commented, these movements will constitute fine adjustments to the policy rate as part of an "active management" phase in the ongoing monetary tightening cycle.
- **We stick to our view that Banxico will likely start to "fine-tune" the monetary policy stance and cut the policy rate by 25 bps to 11.0% in 1Q24** to avoid an unwarranted increase in the real ex-ante policy rate. Yet, the odds that Banxico might delay the first cut to March increased somewhat after today's meeting following Banxico's slight upward revision to its core inflation path, which financial markets seem to have priced in as the USDMXN declined by around 10 cents immediately following the statement release. Although we continue to think that Banxico should not skip rate cuts at any meetings next year, its cautiousness, hawkishness, and recent hints suggest that consecutive rate cuts are unlikely at the start of the gradual easing cycle. **We anticipate a very gradual easing cycle due to Banxico's cautiousness. We expect Banxico to bring down the policy rate to 9.0% by year-end 2024.**

Banxico left its headline inflation path mostly unchanged…

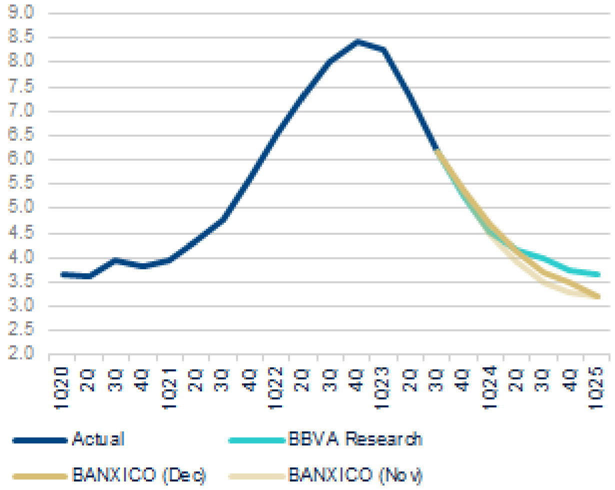
Figure 1. **HEADLINE INFLATION OUTLOOK**
(YOY % CHANGE, QUARTERLY AVERAGE)



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

… but revised somewhat up its core inflation forecasts, bringing its 2024 path closer to ours

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



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

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