

# Mexico Flash

In spite of a greater concern on domestic activity and a better inflation outlook, a rate cut seems to depend on a greater impairment of economic activity

Based on the balance of risks of domestic activity and inflation, the statement could suggest an additional rate cut. However, the policy paragraph does not contain the imminent rate cut signals that the central bank used in the January statement. The activity figures in the coming months will be key to the monetary stance.

- Banxico intensifies its negative tone regarding domestic activity. It stresses that the pace and depth of the economic slowdown have increased the downside risks.
- The tone on inflation is positive as the balance of risks has improved. However, it is worth noting that when discussing the upside risks on inflation Banxico stresses its transitory nature given its reluctance to accommodate second round effects stemming from supply shocks.
- The wording of the closing paragraph on monetary policy was mostly unchanged from the 7 June statement as it only added a reference to volatility in international financial markets
- Considering that the paragraph on monetary policy does not seem to open the door to an additional rate cut in coming months, the likelihood of further easing in September anticipated in our base scenario seems to have decreased. Going forward, the probability would increase with greater economic weakness and/or a relative tightening of the monetary stance.

Table 1  
Highlights from last statements

|                                 | June 7th   | July 12th  | Assesment  |
|---------------------------------|--|--|--|
| <b>Global context</b>           | <ul style="list-style-type: none"> <li>• Downward <b>risks on global activity remain</b></li> <li>• The weakness of global economic activity has increased</li> </ul> <p>Lower inflation outlook in most countries</p>   | <ul style="list-style-type: none"> <li>• <b>Downward risks</b> on global activity <b>remain</b></li> <li>• The weakness of global economic activity <b>has increased</b></li> <li>• Lower inflation outlook <b>in most countries is expected</b></li> </ul>  | <b>Caution regarding downward risks on global economic activity.</b> |
| <b>Domestic activity</b>        | <ul style="list-style-type: none"> <li>• Downward risks on domestic activity have intensified</li> <li>• Domestic activity has observed an important deceleration</li> </ul>   | <ul style="list-style-type: none"> <li>• <b>Downward risks</b> on domestic activity <b>have intensified, given the speed and depth of the deceleration</b></li> <li>• <b>Deceleration worsened significantly in 2Q13 by a significant slowdown in exports and weak domestic demand</b></li> <li>• <b>Economic slack has increased</b></li> </ul> | <b>Increased concern due to the deepening of the deceleration</b>    |
| <b>Inflation</b>                | <ul style="list-style-type: none"> <li>• A slight inflation reduction is expected in June, but the downward trend will steepen from July onwards. Inflation will be between 3 and 4% in the 2H13 and close to 3% during 2014.</li> <li>• Core inflation will be even below 3% during most of 2013 and 2014.</li> <li>• Upward risks on inflation prevail (supply shocks), but the materialization of downward risks on economic activity could offset them.</li> </ul> | <ul style="list-style-type: none"> <li>• The balance of risks for inflation <b>has improved</b></li> <li>• <b>Inflationary effects from the recent currency depreciation are not expected</b></li> <li>• Downward expectations on inflation prevail</li> </ul>   | <b>Improved balance of risks</b>                                     |
| <b>Monetary policy decision</b> | 0.00   | 0.00   | <b>The room for an additional rate cut is limited</b>                |
| <b>MP rate</b>                  | 4.00   | 4.00   |  |

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