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GLOBAL ECONOMICS

LATAM DAILY

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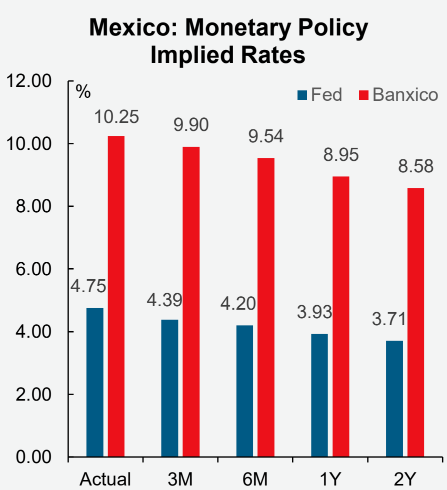
Chart 1



Sources: Scotiabank Economics, Bloomberg.

Latam Daily: Mexico's Monetary Policy Minutes; Peru Previews November Inflation

- **Mexico: Diverging opinions despite a unanimous decision**
- **Peru: Inflation set to bounce just a bit in November**

MEXICO: DIVERGING OPINIONS DESPITE A UNANIMOUS DECISION

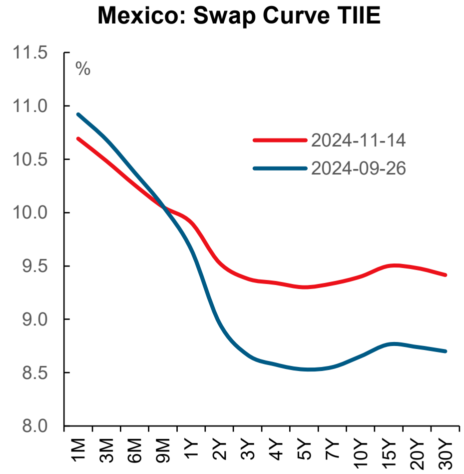
The minutes from Banxico's November 14th meeting detailed the discussion on inflation and monetary policy within the Governing Board, where a rate cut of 25 basis points was voted unanimously to reach a reference rate of 10.25% (chart 1). Overall, the arguments of the Board members turned around the disinflationary process. However, the Governing Board appears divided in opinions. Some members proposed higher cuts in the coming meetings, while others prefer to calibrate the cuts to achieve convergence to the inflation target.

Regarding the Mexican economy, comments highlighted the higher-than-expected growth in Q3-2024, surpassing the previous quarters. Members mentioned that services contributed the most to growth, while industrial activity did so to a lesser extent due to stagnant manufacturing. Construction has also been stagnant, and mining remains in contraction. They noted that private consumption improved compared to the second quarter, led by imported goods and services consumption, while domestic goods were perceived as weak. On the other hand, all members mentioned that investment has slowed, with a decline in public investment and a slight increase in private investment. The Board indicated that they expect a slower pace of economic activity for 2025 and 2026, owing to lower private investment and weaker consumption (chart 2). Comments also referred to the uncertainty regarding the changes that the United States will take in its economic policy. On the employment side, it was noted that it has remained strong, and the unemployment rate is still at low levels. However, the labour market is already showing some slowdown, observed in most sectors and regions of the country.

Regarding inflation, the members pointed out that the October rebound was due to the non-core component, mainly agricultural products, while the core component maintained a downward trajectory. In our opinion, the document shows a certain confidence that the disinflationary process will continue downward, despite the balance of risks remaining tilted to the upside. In this regard, the minutes mentioned the stickiness of the services component, considering that it remains at high levels despite being below 5.0% for the first time since July 2022. Moreover, several members maintained some concern about labour cost pressures, particularly in services. Regarding inflation expectations, some members mentioned that these have remained relatively stable, although others reiterated that the central bank's forecasts diverge from those of private sector analysts and market-implied expectations. Looking ahead, the majority of the Board agreed that one of the upside risks is also the possibility of a greater depreciation of the USDMXN, in addition to the persistence of services. Some members pointed to the possibility of new inflationary shocks in agricultural products in the coming months, the risk of trade policies negatively impacting prices, the risk of a higher fiscal deficit, and the resilience of consumption. On the downside, several members pointed to the possibility of lower economic activity, an argument in which some of them seem to base their opinion on a less restrictive rate, as well as the possibility of a lower-than-anticipated exchange rate pass-through.

In the monetary policy discussion, despite the unanimous decision, we perceive different opinions on the inflation outlook and policy direction. In this regard, two members believe that inflationary pressures are easing, and going forward, these pressures could dissipate, allowing for continued rate adjustments in the upcoming meetings. Those members also mentioned there is room to increase the magnitude of future cuts, as Governor Victoria Rodriguez already mentioned last week in a press interview. On the other hand, the rest of the Board was perceived as more cautious, as they consider that the risks ahead remain to the upside, while mentioning that it is not clear yet that the downward trend of the services component will continue, and that pressures could persist due to consumption resilience resulting from a solid labour market and wage increases. Some members were also concerned about the divergence between inflation expectations of private analysts and the central bank's projections. However, the Board stated that there is room for additional adjustments, although still depending on new available data, as the balance of risks remains biased to the upside and inflation expectations persist above the 3.0% target.

Chart 2



Sources: Scotiabank Economics, Bloomberg.

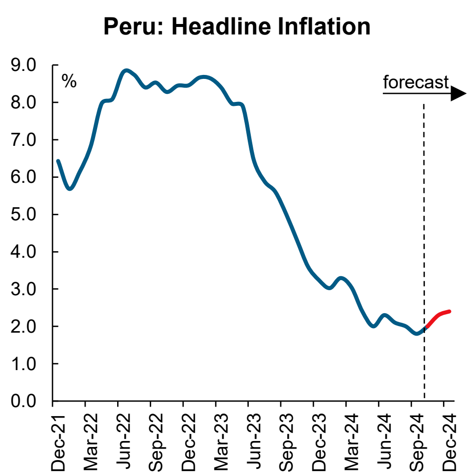
Looking ahead, we maintain our perspective that Banxico will repeat a 25 basis points cut at the December 19th meeting. However, going forward, uncertainty related to both external and internal events could result in a combination of diverse scenarios that will make it difficult to forecast inflation and monetary policy response. In this sense, we anticipate that convergence to the inflation target will take longer than expected, despite the economic slowdown, making higher cuts in the near term unlikely, and doubtful that the reference interest rate will end 2025 below 8%.

—Rodolfo Mitchell, Brian Pérez & Miguel Saldaña

PERU: INFLATION SET TO BOUNCE JUST A BIT IN NOVEMBER

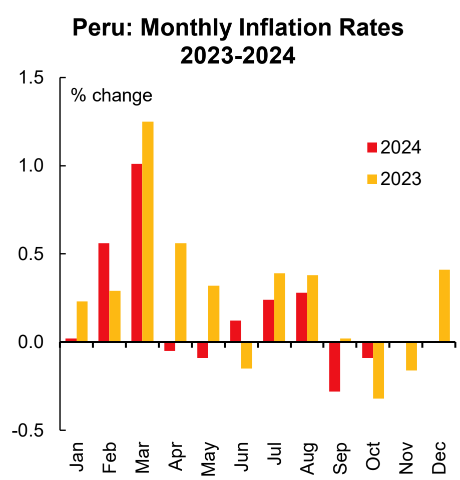
The figure for November inflation will be published on Sunday, December 1st. We expect monthly inflation to be close to 0.2%. This should take yearly inflation up from 2.0% last month, to 2.3%–2.4% in November. This should not be too much of a concern for the BCRP because the reason is a low base, namely, monthly inflation was negative in November 2023. None of this is surprising, and is in line with our long-standing full-year forecast of 2.4% (charts 3 and 4).

Chart 3



Sources: Scotiabank Economics, BCRP.

Chart 4



Sources: Scotiabank Economics, INEI.

The BCRP is well aware of the base effect. However, it may take the uptick as an opportunity to avoid reducing the reference rate in December. The BCRP has already signaled that it is nearing the end of its rate reduction cycle. Given this, we expect two more reductions in the coming months, until a terminal rate of 4.50% is reached. But, there is no hurry in reaching this terminal rate. December might be a good month to pause. Having said that, the arguments for a pause are of convenience rather than expedience, and, with no compelling pressure to be decisive, the BCRP decision could go either way.

What will also be released on Sunday is mining GDP and fishing GDP figures for October, as well as other early growth indicators. What will be of particular interest is how strong fishing growth is, given that were in the middle of a main fishing season, and the preliminary information we are receiving is that things are going very well. The early indicators will give us some incipient clarity on how strong Q4 GDP growth will be. Our forecast is for 3.3% YoY growth. However, Finance Minister José Arista has stated that GDP growth could come in at 4.0%. We shall see.

—Guillermo Arbe