

Mexico: Banxico Unexpectedly Raised Overnight Rate to 4.25% from 4.00%

In a split decision, the Board of Mexico's central bank (Banxico) delivered a surprise 25 bps hike, raising the overnight rate from 4.00% to 4.25% (chart 1). Two of five board members voted to hold. Factoring into the decision was the possibility that central banks from emerging markets would start tightening earlier than anticipated. The board now sees balanced risks to growth, even if Banxico still sees slack in the economy for the remainder of the year.

Inflation shocks are seen by Banxico as driven by transitory factors, but the release highlighted the continued increase in inflation expectations (a print earlier today showed a 6.02% y/y headline inflation, versus 5.80% y/y consensus and 5.89% y/y previous). It is worth noting that since the *Inflation Report* published this month, the Board announced it now sees inflation converging to target one quarter later (Q3-2022, as opposed to Q2-2022 a couple of weeks ago).

The most relevant indication of whether this means Banxico is entering a tightening cycle will be 2022 inflation expectations. The most relevant upcoming inflation survey will likely be Banxico's, whose survey responses can still be modified by today's deadline, giving the central bank insights into pre and post-decision numbers. A potentially relevant reason behind Banxico's reluctance to commit to a tightening cycle is the divided opinion among its Board members.

With today's development, we move up our policy rate expectation to 4.50% for the end of 2021, where we previously expected a 4.00% rate, implying another hike of 25 bps during the rest of the year.

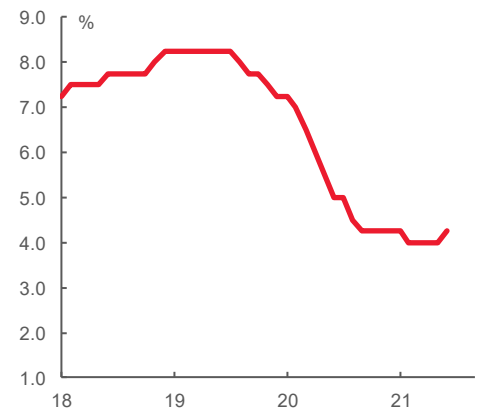
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Chart 1

Mexico: Overnight Rate



Sources: Scotiabank Economics, Banxico.

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