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Mexico—Another 75 bps... Was It the Last One of this Magnitude?

- Banxico hiked another 75 bps, following the Fed, but is keeping its options open for smaller increases going forward.

Banxico’s Board of Governors unanimously agreed to **raise** the monetary policy interest rate by 75 bps, for a second time, to 8.50%. Following the last decision and the hawkish tone of the minutes, the market did not doubt that another 75 bps increase would follow, with all 24 economists surveyed by Bloomberg anticipating the move. However, with a somewhat less aggressive tone than in the previous decision, Banxico indicated that it will evaluate “the prevailing circumstances” in its subsequent decisions, leaving the door open for smaller increases going forward.

The central bank revised upwards its inflation forecasts for the fifth consecutive time. In its new scenario, inflation peaks at 8.5% (8.1% previously) in the third quarter of 2022, with the largest revisions concentrated between Q4-2022 and Q2-2023, and of up to 80 bps (interestingly, to core inflation), before gradually converging to 3.1% in the first quarter of 2024, as indicated in the March decision, and which has since been unchanged.

Conditions warranted another 75 bps hike: inflation continues to accelerate (although July’s m/m inflation moderated slightly, in annual terms it remains at more than 20-year highs) along with the continued deterioration in expectations (charts 1 and 2), which have consistently increased with each survey; accelerated tightening in global financial conditions, particularly the Federal Reserve’s second 75 bps hike and its commitment to bring inflation to target; and reduced slack in certain sectors of the economy.

Although the balance of risks continues to be skewed to the upside for inflation, the recent deceleration in energy prices could be an indication that we are close to the peak and inflation will begin to fall in the last quarter of this year, as Banxico anticipates. We expect a 50 basis point increase in September (especially after the word “forceful” no longer appears in the statement) and that the central bank will take the rate to 10.00% by the end of 2022. While supply-side price pressures may begin to recede, Banxico and other central banks, cannot let their guard down yet, and will have to continue to demonstrate that they will do whatever it takes to return inflation to target.

Chart 1

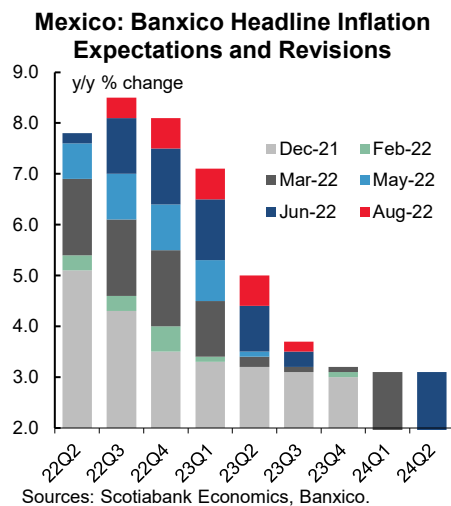
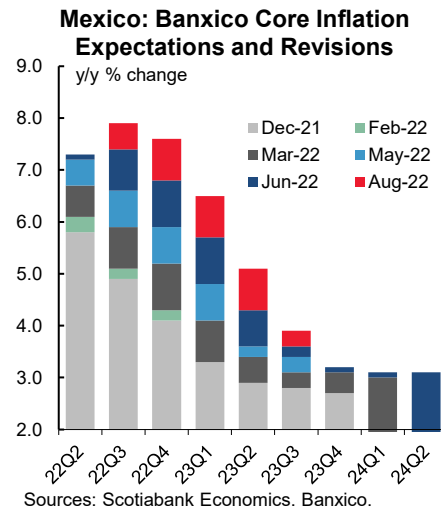


Chart 2



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