Scotiabank.

GLOBAL ECONOMICS

LATAM FLASH

January 5, 2023

Contributors

Luisa Valle, Deputy Head Economist
+52.55.5123.1725 (Mexico)
lvallef@scotiabank.com.mx

Miguel Saldaña, Economist
+52.55.5123.1718 (Mexico)
msaldanab@scotiabank.com.mx

Mexico—Minutes: Very Close to the End of Synchronization with the Fed

In the **minutes** corresponding to the December decision, Banxico decided to reduce the pace of increases in a 4-to-1 vote (50bps vs. 25bps), opting for **50 basis points to 10.50%.** For now, we expect Banxico **to raise 25bps in the February decision and maintain a tightening stance through 2023.** Going forward, we cannot rule out another hike in the March decision, and the following core inflation readings, as well as the dynamics of the labor market under the minimum wage hike, will be crucial.

In the **external environment**, most agreed that the probability of a global recession in 2023 remains high, mainly due to geopolitical tensions and tightening financial conditions. In this sense, it is expected that reference rates will remain at elevated levels for a long period of time. However, they mentioned that lower pressures on commodity prices and supply chains can already be observed, contributing to a decline in headline inflation in some countries. Additionally, according to a member of the Board, the risk of inflation is declining more rapidly in the United States than in Mexico. Nonetheless, an environment of uncertainty prevails, where a stronger dollar could impact global financial stability, increasing borrowing costs and leading to capital outflows in emerging markets.

Regarding **economic activity in Mexico**, most agreed that it has already reached pre-pandemic levels, albeit with a mixed recovery, supported by services and the export sector. However, the weakness in investment and construction, combined with lower global growth prospects, maintains the growth outlook for Mexico in 2023 with a downward bias. **Regarding the minimum wage increase, most agreed that it could have an impact on inflation**, to which one member added that there is a risk of companies passing on their cost increases to consumers in the event of a mismatch between wage revisions and productivity.

On **inflation**, all members highlighted that the decrease in headline inflation was due to the non-core component, with reductions in energy and some agricultural products. However, core inflation maintained its upward trend, pressured by both external factors arising from the pandemic and the conflict in Europe, and internal factors, derived from wage revisions. In this sense, one member highlighted that it is necessary to pay greater attention to the measurement and follow-up of internal inflationary pressures, which another member pointed out are increasingly evident, especially in consumption. In this sense, another member commented that their prevalence could complicate the convergence of inflation, whose expectations have remained at high levels. The text also noted a still-uncertain environment despite the expected moderation in inflationary shocks. It is clear to us that the Board continues to be concerned about core inflation and the deterioration of inflation expectations, however, **several comments lead us to believe that in February we will see another decrease in the pace of Banxico's rate hikes and most likely the end of the synchronization with the Federal Reserve.**