



Outlook and perspectives for the Mexican economy

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Outline

1 External conditions

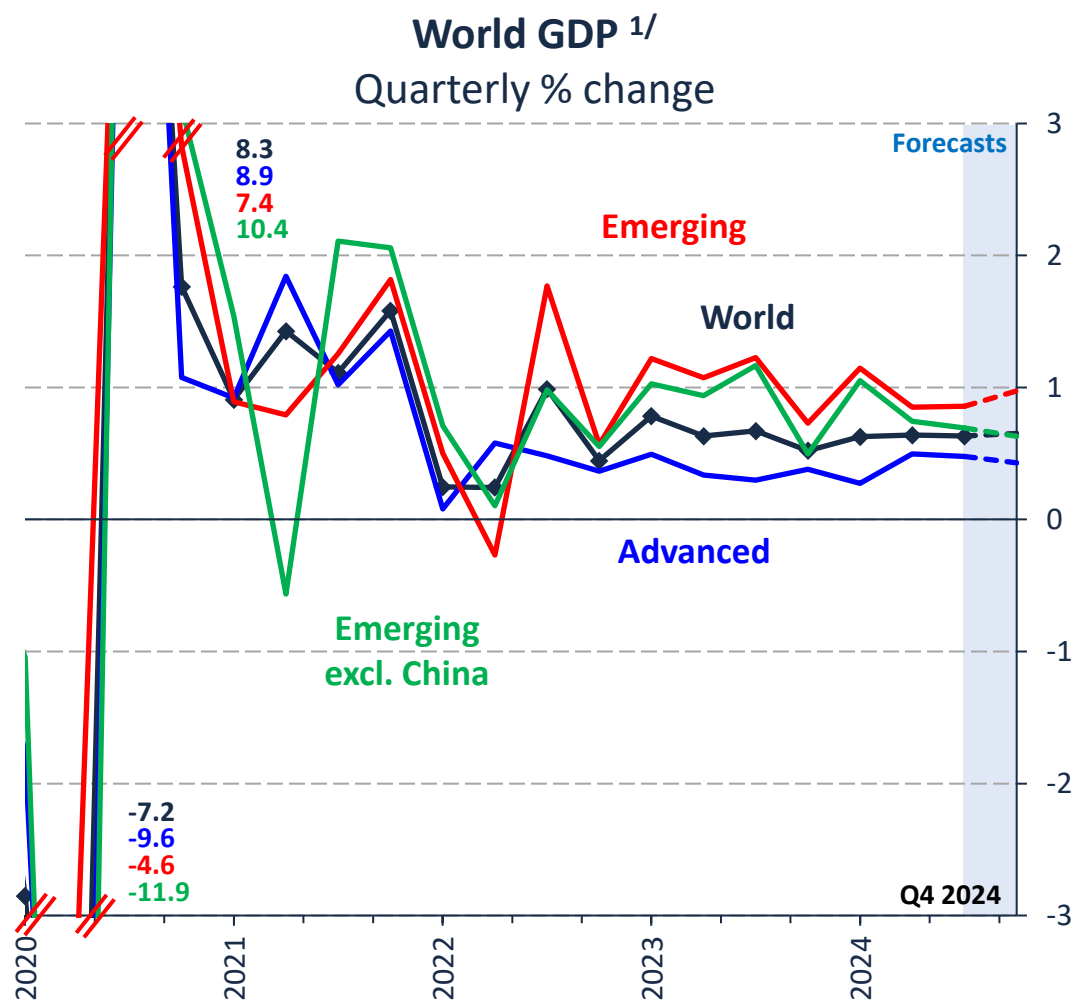
2 Current situation of the Mexican economy

3 Inflation and its determinants

4 Monetary policy

Global economic activity has expanded at a similar pace to previous quarters, although, with differences across economies.

World Economy

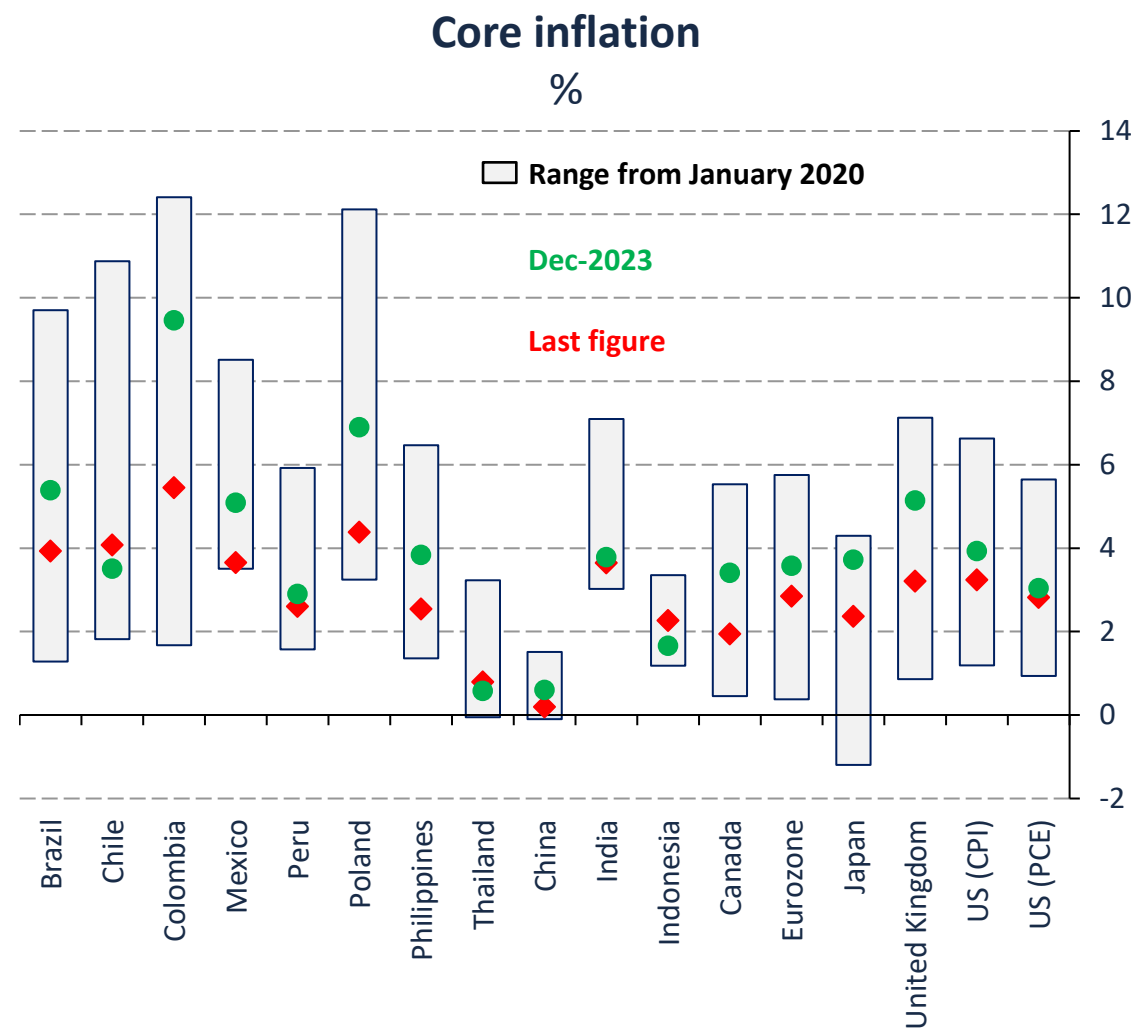


1/ On October 28, a change in the seasonal adjustment methodology was implemented for the source (Haver Analytics) of the quarterly GDP series for China, expressed in trillions of dollars at constant prices and 2010 exchange rates. This series is used for the construction of global GDP aggregates.
Note: The dashed lines represent forecasts for the fourth quarter of 2024.
Fuente: Haver Analytics y JPM.

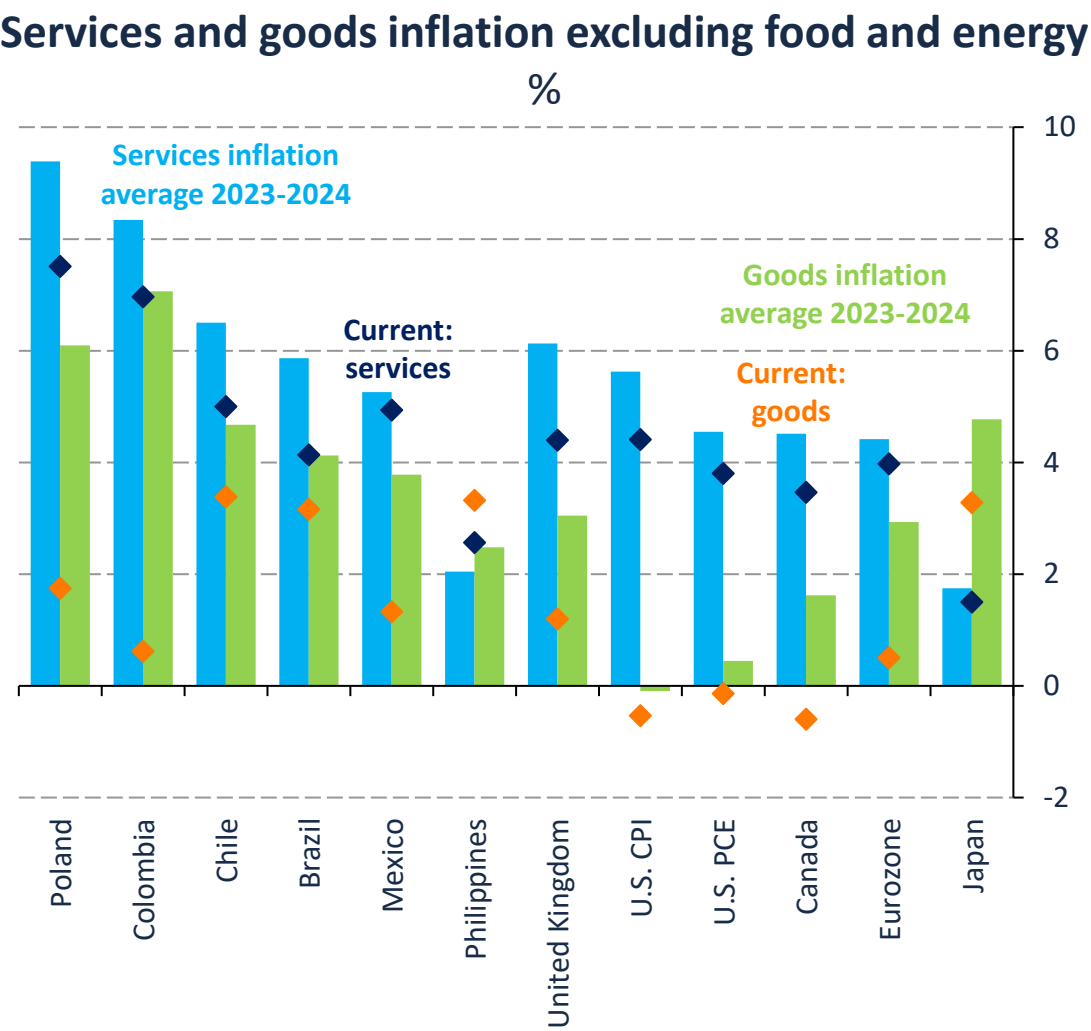


Source: International Monetary Fund, WEO, October 2024.

Global disinflation has shown a remarkable progress. Despite some rebound in headline inflation during 2024, due to energy and food prices in some economies, core inflation continues to decline steadily.



Source: Haver Analytics and central banks' web pages.

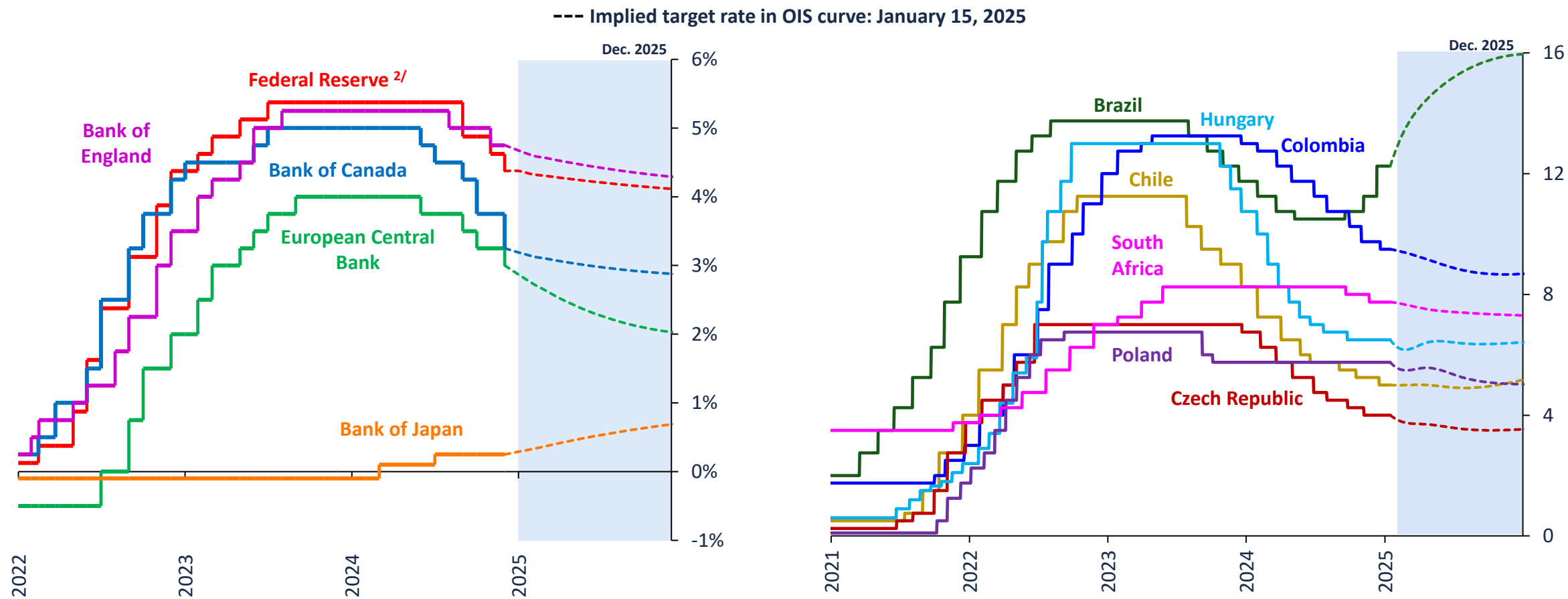


Note: Figures are estimates. For Mexico, Chile, and Colombia, the figures are those reported by their national statistical institutes. Source: Banco de México with information from BLS, BEA, Eurostat, ONS, e-Stat, Statistics Canada, Haver Analytics, Central Bank of Chile, and INEGI.

Heterogeneity in monetary cycles persists; however, going forward, central bank decisions will weigh the need to avoid excessively restrictive monetary stances in light of the progress in disinflationary processes.

Reference Rates and Implied Trajectories in OIS Curves ^{1/}

%



1/ OIS: Fixed-for-floating swap where the fixed interest rate is the overnight effective reference rate.

2/ The observed federal funds rate corresponds to the average between the lower and upper bounds of the target range, for Europe the deposit facility rate is used and for Japan the upper limit of the target rate.

Source: Bloomberg.

Outline

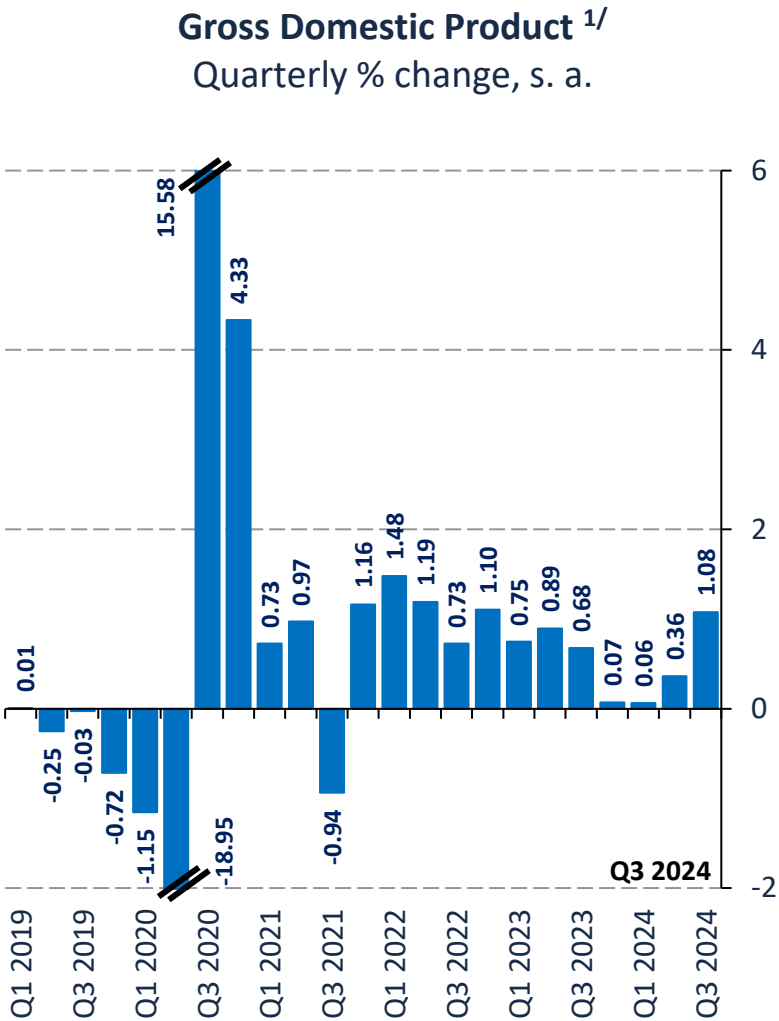
1 External conditions

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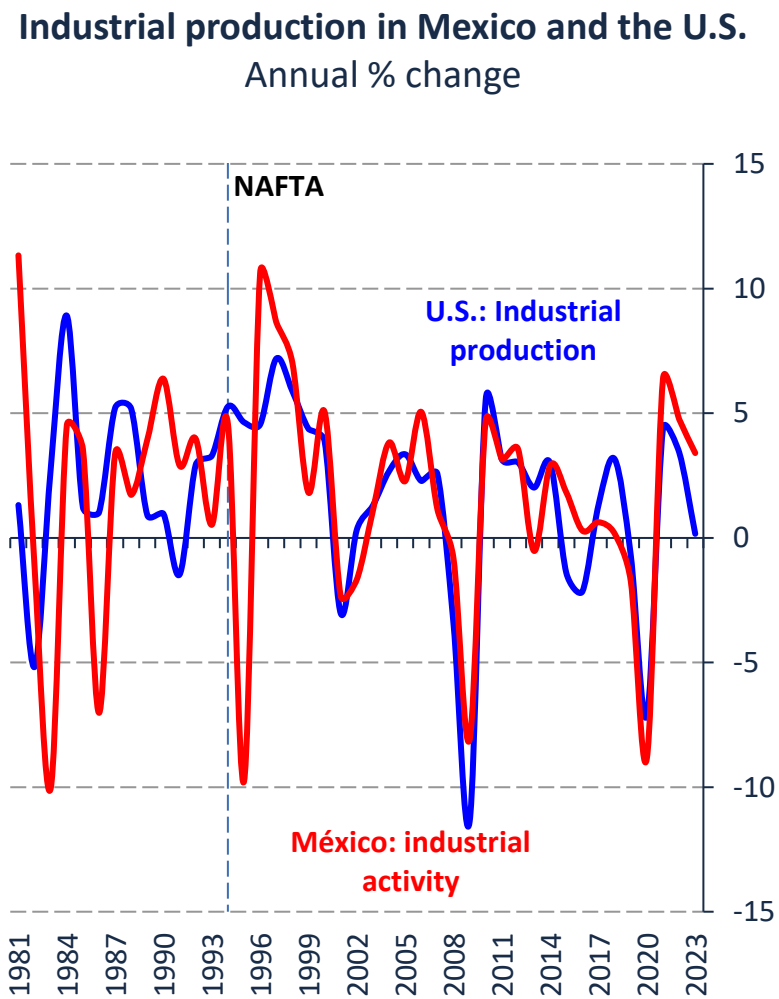
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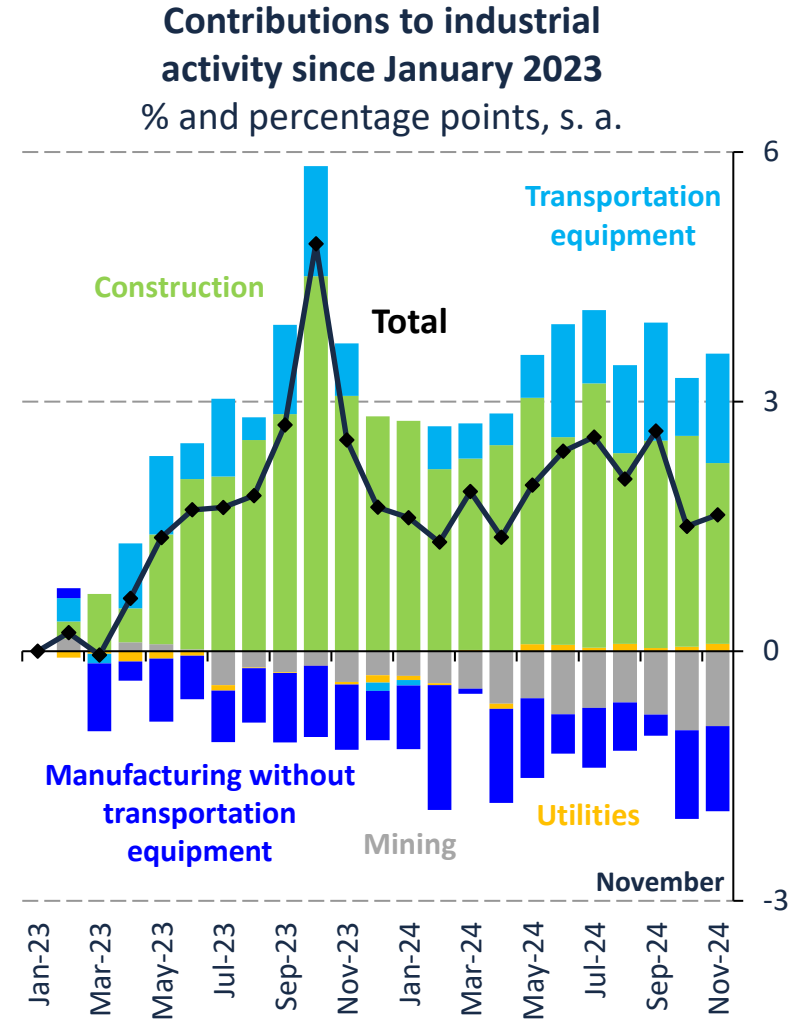
Economic activity in Q3 2024 picked up, partially driven by primary sector activities, following a period of pronounced weakness during the previous three quarters.



s. a./ Seasonally adjusted. 1/ The range of the chart was reduced to facilitate its reading. Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.



Source: Federal Reserve and INEGI.

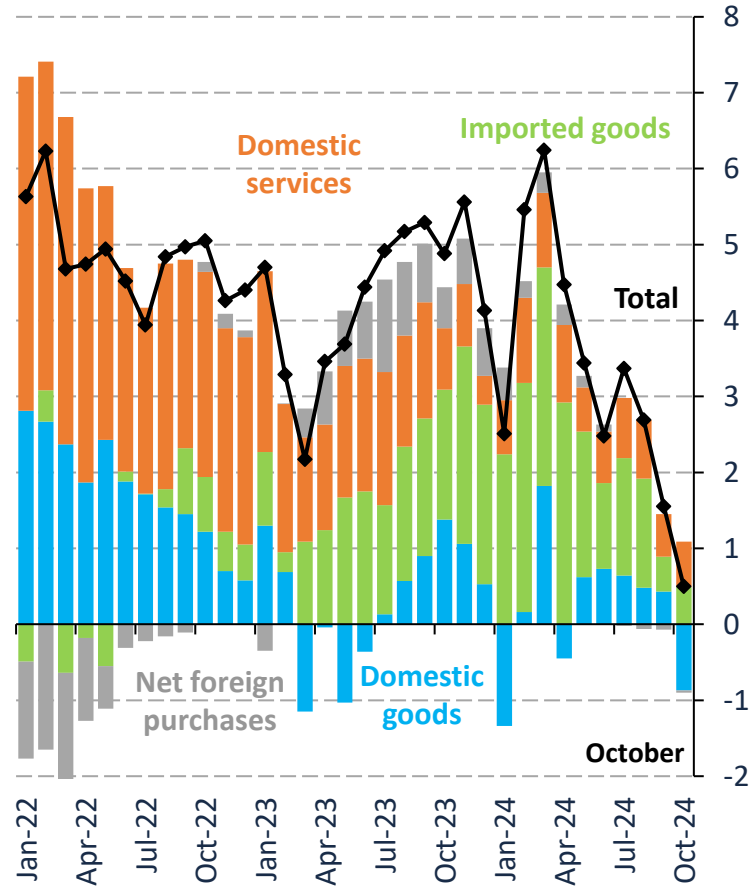


s. a./ Seasonally adjusted figures. Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

Domestic consumption of services and goods has continued moderating; investment has remained sluggish, while manufacturing exports observed a slight rebound.

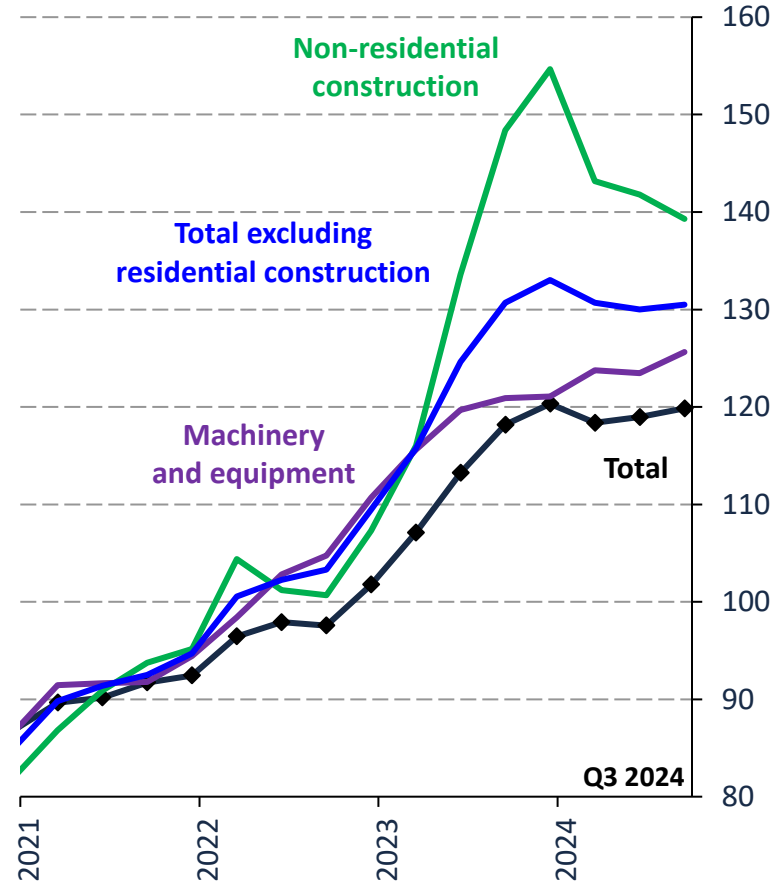
Contributions to total private consumption, s. a. ^{1/}

Annual % change and percentage points



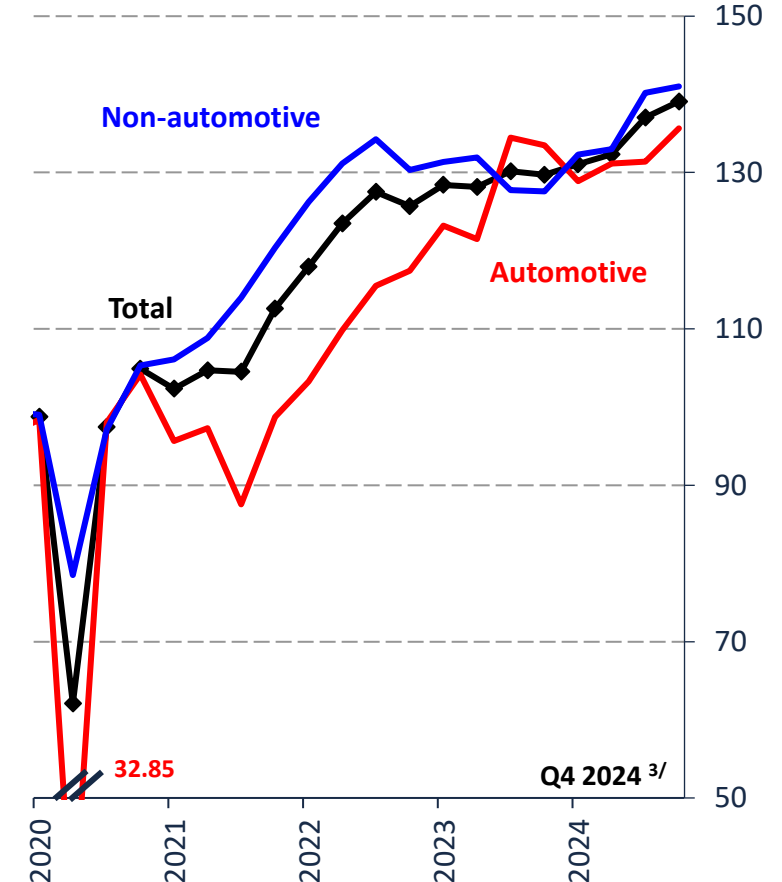
s. a. / Seasonally adjusted figures. Note: Prepared and seasonally adjusted by Banco de México. Differences due to the independent deseasonalization of the components. 1/ Contributions are estimated from non seasonally adjusted data. Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

Investment
Index 2019=100, s. a.



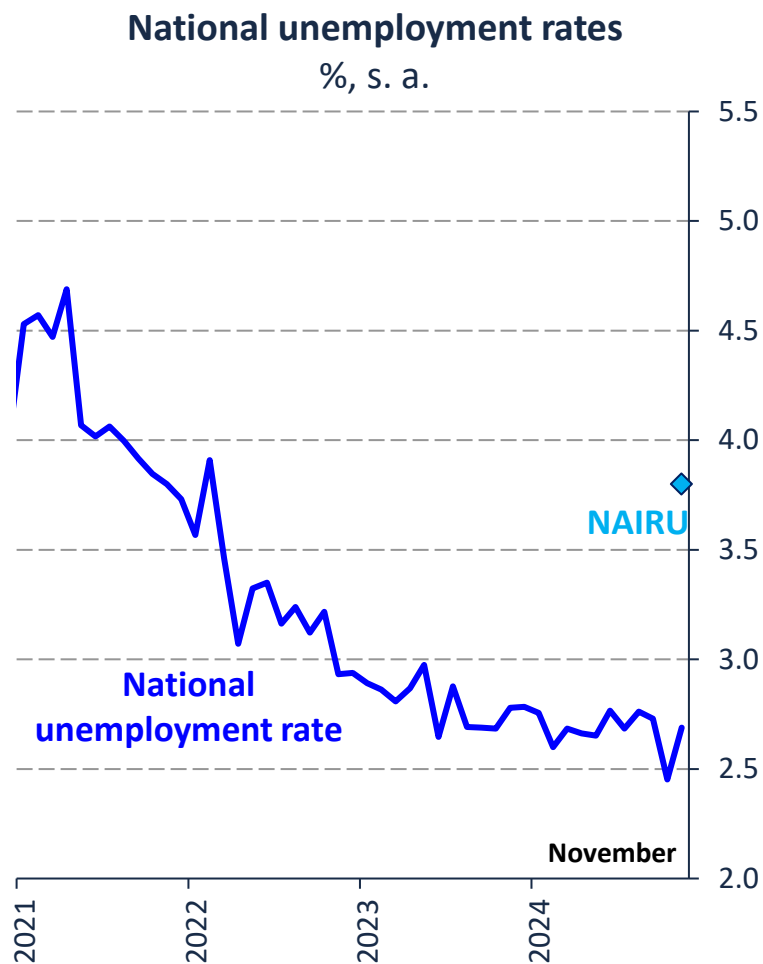
s. a. / Seasonally adjusted figures.
Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

Manufacturing exports ^{2/}
Index 2019=100, s. a.

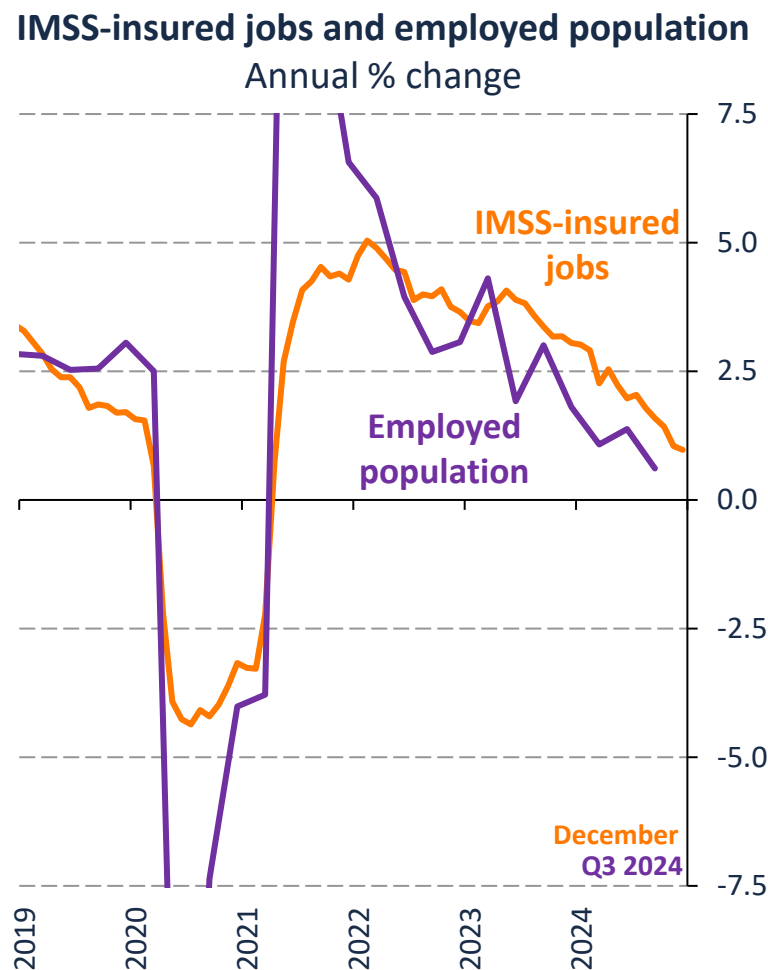


s. a. / Seasonally adjusted figures. 2/ Based on current US dollars.
3/ The Q4 2024 figures represent the average of October and November.
Note: The range of the chart has been reduced to facilitate its reading.
Source: Banco de México with data from PMI Comercio Internacional, S.A. de C.V., SAT, SE, Banco de México and INEGI. Mexico's Merchandise Trade Balance. SNIEG. Information of National Interest.

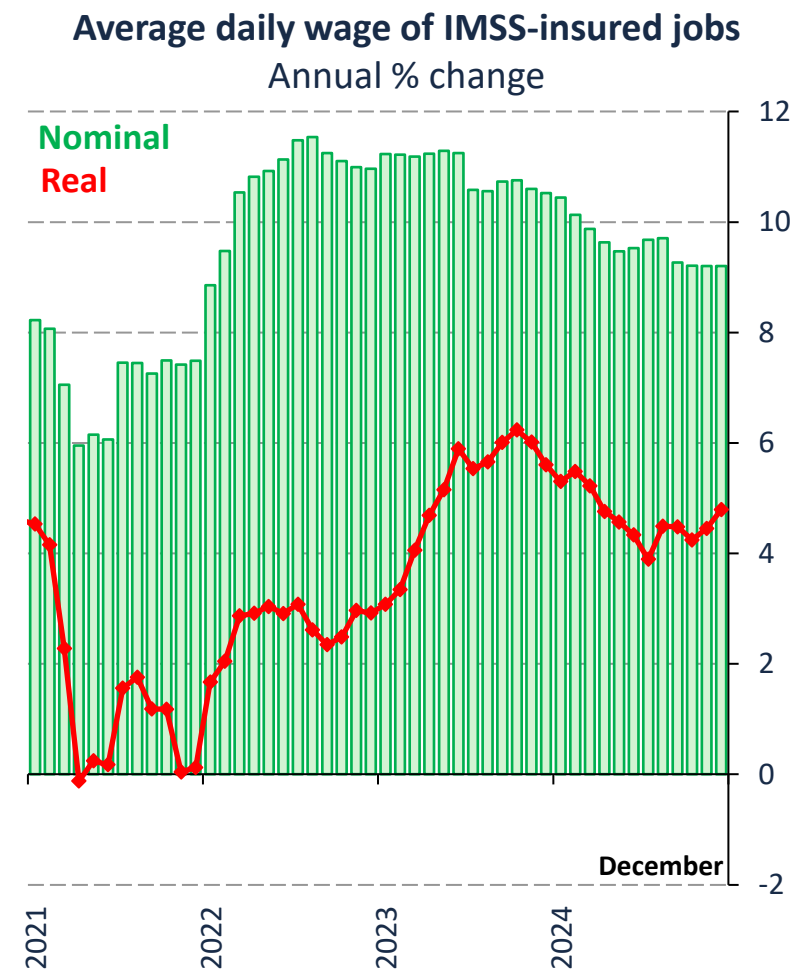
The labor market has remained solid. Still, some signs of labor market cooling have become more evident.



s. a. / Seasonally adjusted figures.
Source: Prepared by Banco de México with data from INEGI (ENOE).



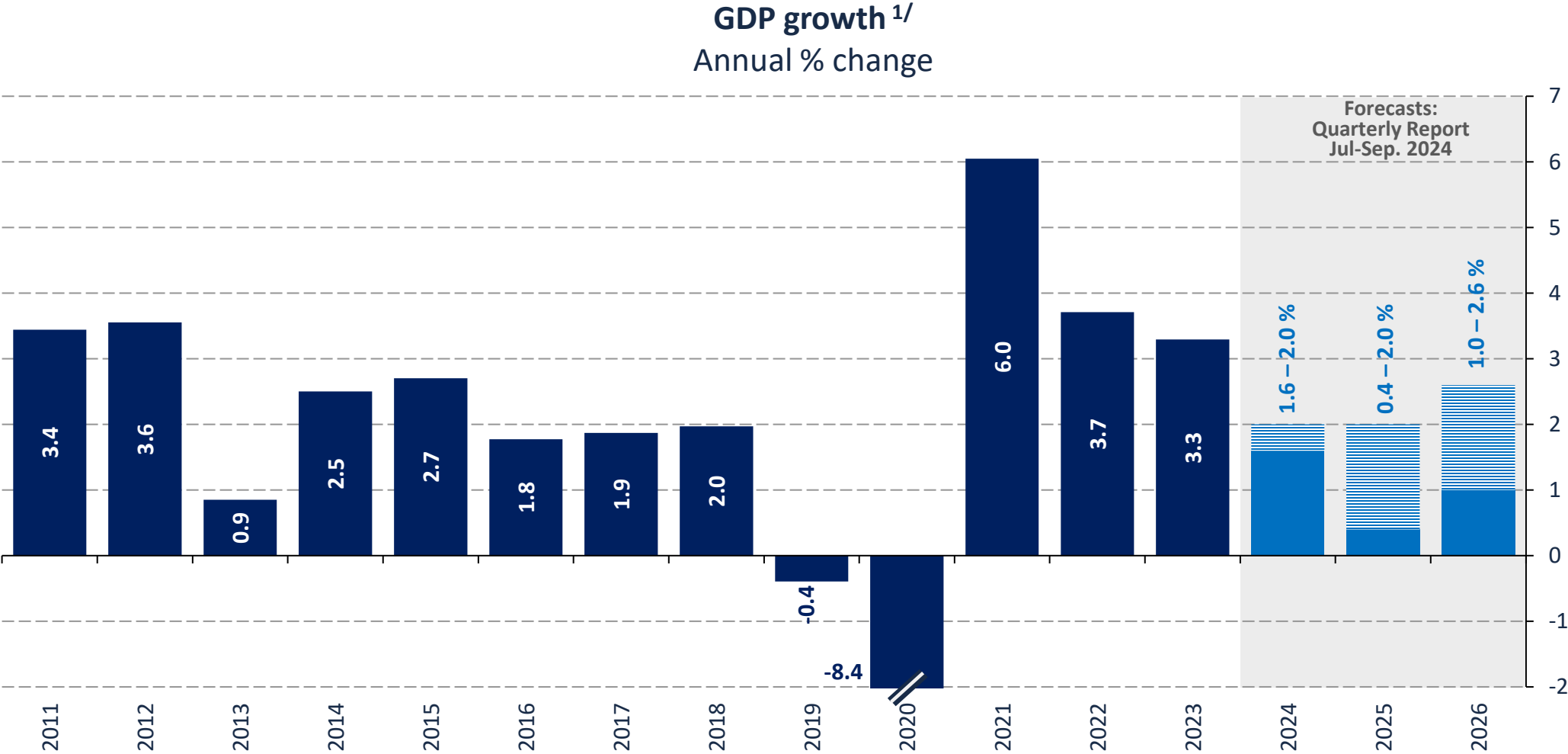
Source: Prepared by Banco de México with data from INEGI (ENOE) and IMSS.



Source: Prepared by Banco de México with data from INEGI (ENOE) and IMSS.

It is anticipated that the economy will continue expanding, although at a slower pace.

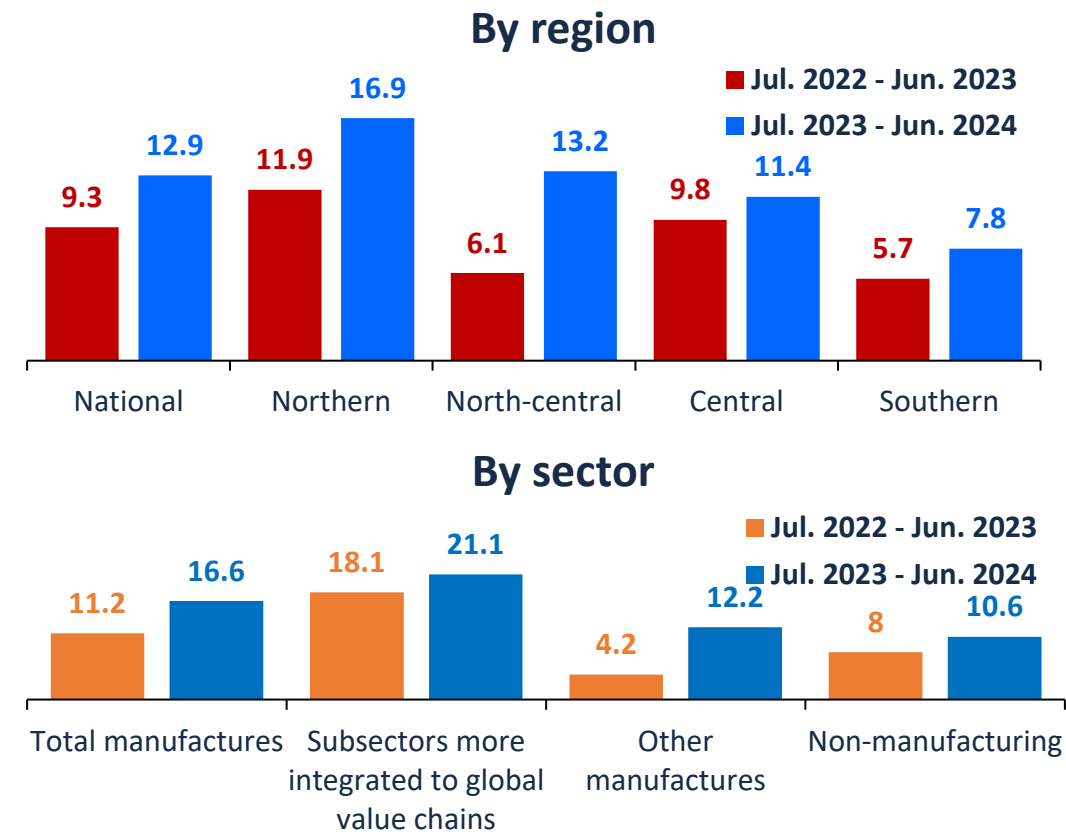
Economic activity outlook



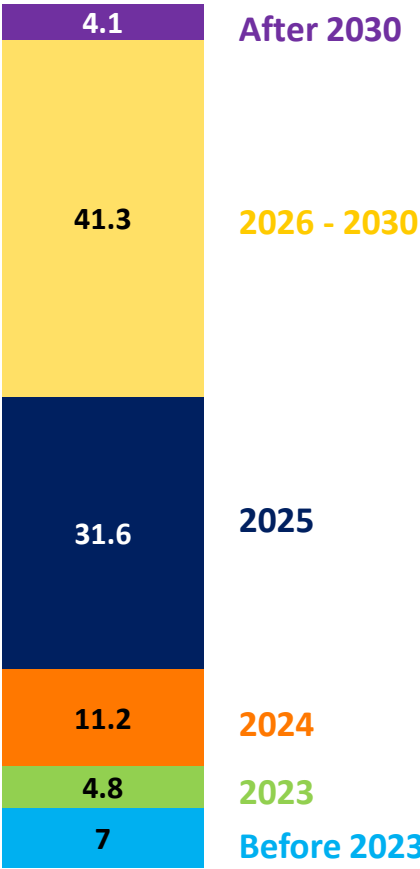
Note: Forecasts with figures without seasonal adjustment. Source: Banco de México.

Although difficult to measure, qualitative information suggests that the impact of the nearshoring process could materialize in the coming years.

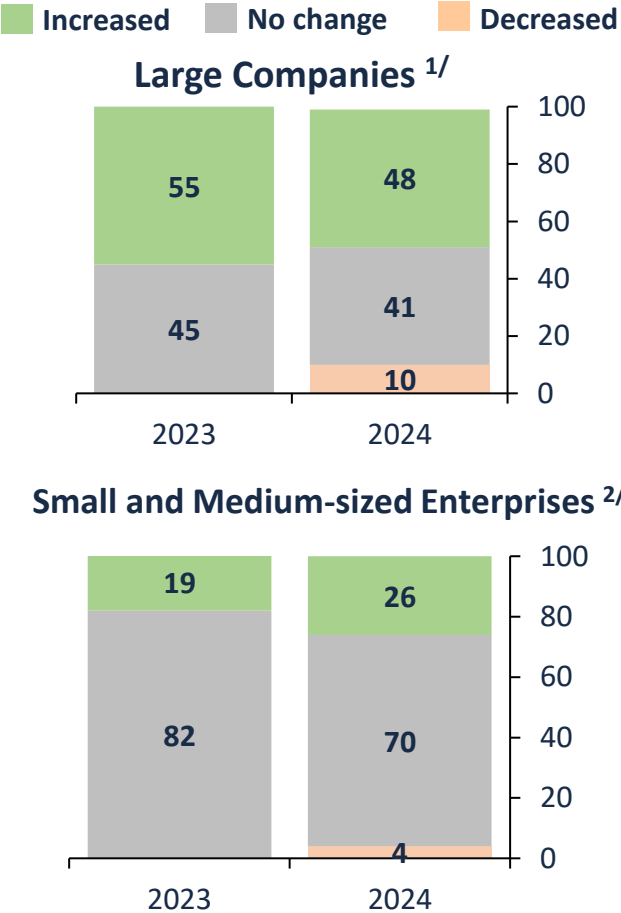
Firms that reported increases in production, sales or investment as a result of nearshoring in different periods
% of firms with more than 100 employees



Period in which the greatest benefit of nearshoring is expected to be observed
% of firms that have observed or expect to see benefits

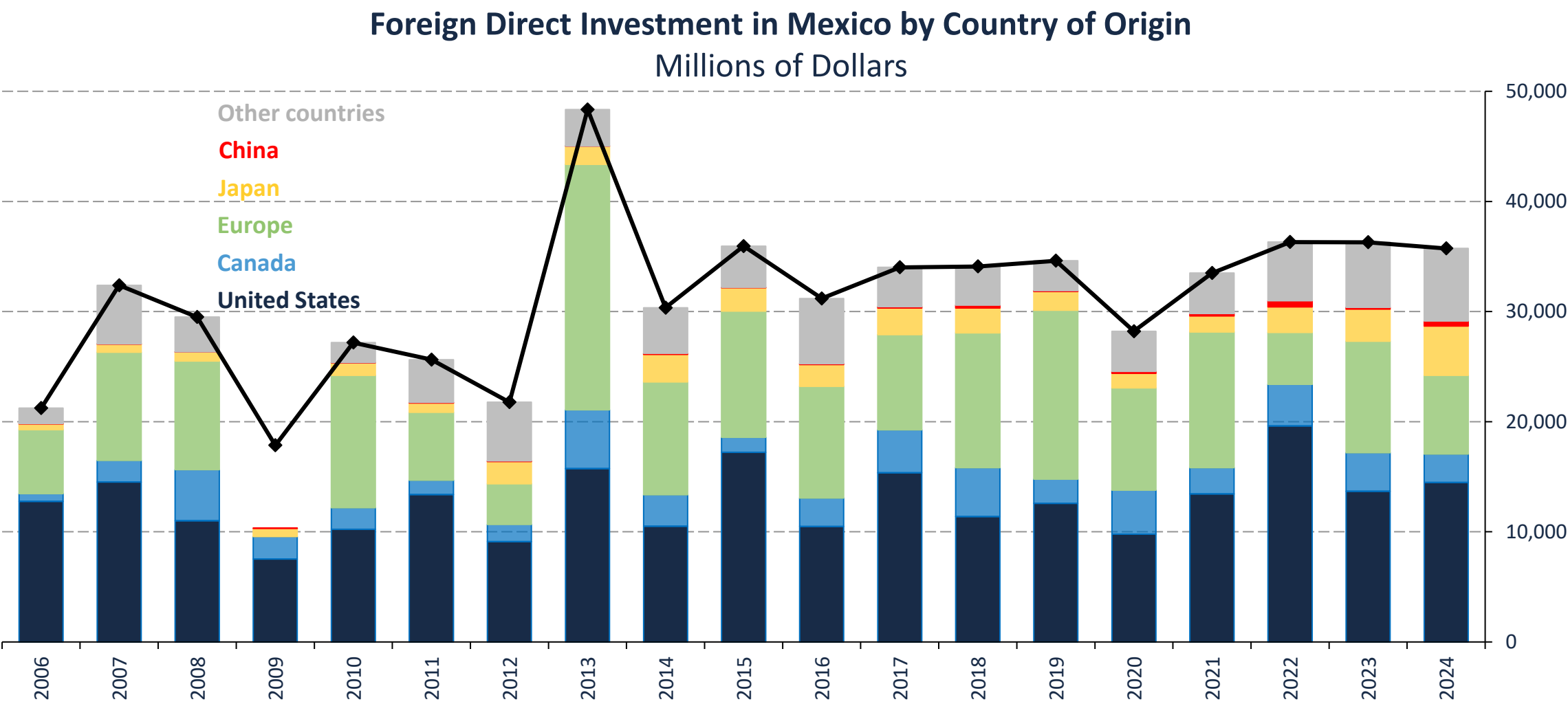


Changes in business credit demand over the last 12 months
% of responses from surveyed banks



Source: Prepared by Banco de México with data from the Monthly Survey of Regional Economic Activity, which is representative of establishments with more than 100 employees in the manufacturing and non-manufacturing sectors at the national and regional levels. The results for groups with greater disaggregation are presented for illustrative purposes, although they are not statistically representative. The manufacturing sector integrated in global value chains groups NAICS subsectors whose share of global manufacturing export value added in total production in 2019 was greater than 10% according to INEGI, and includes the following subsectors: 315, 326, 331, 332, 333, 334, 335, 336, and 339. 1/ The sample includes 19 banks. 2/ The sample includes 19 banks. Source: Banco de México with data from the EnBan Survey for the third quarter of 2023 and the third quarter of 2024.

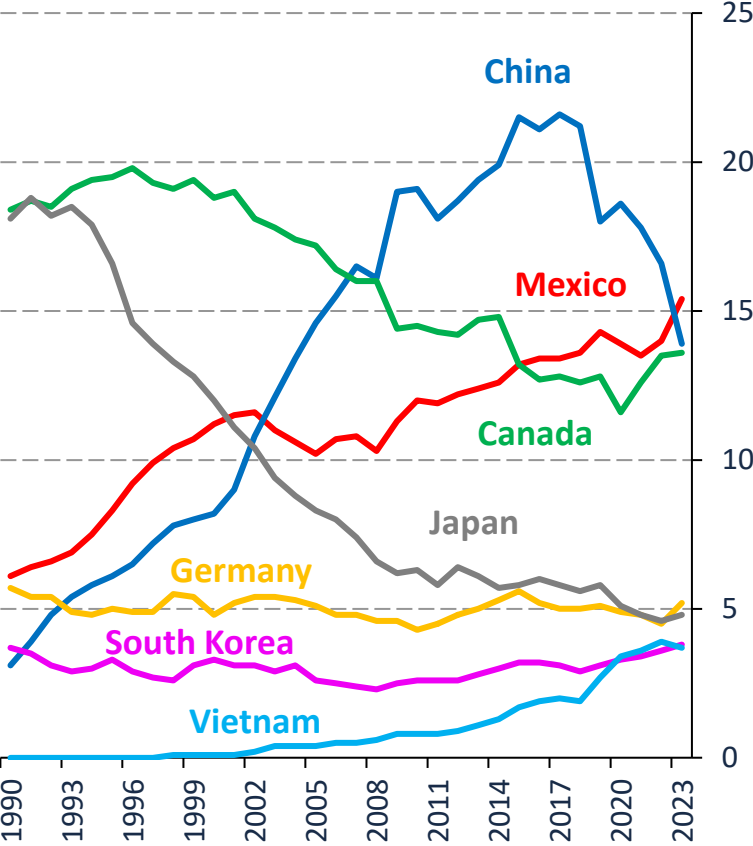
The largest flow of foreign direct investment in Mexico comes from its main trading partners.



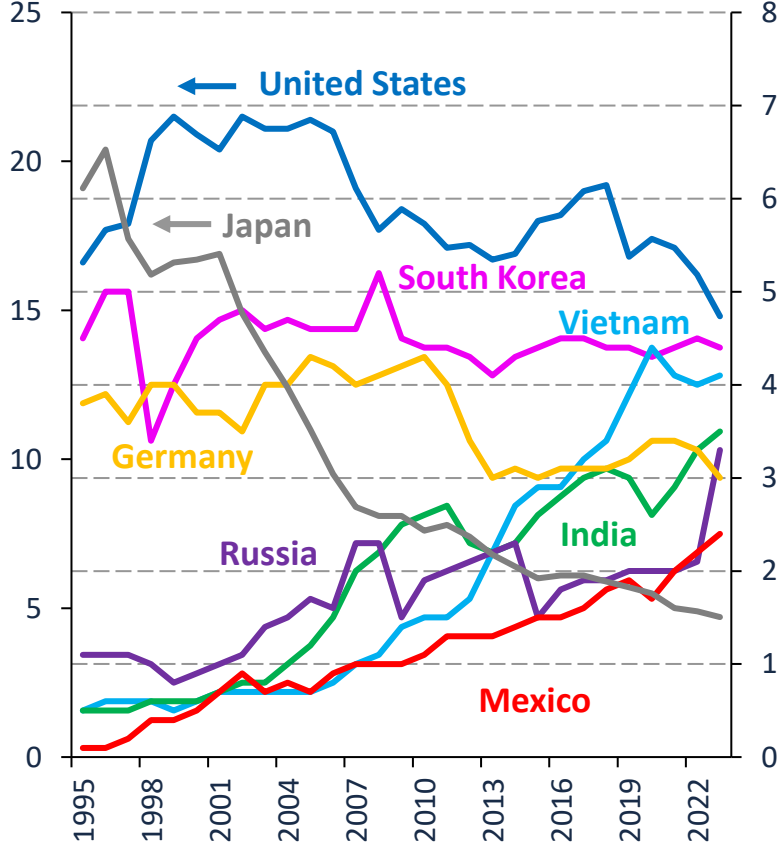
Source: Secretaría de Economía.
Note: The information for 2024 includes figures up to the second quarter.

A very small fraction of U.S. imports corresponds to a potential diversion of Chinese exports through third countries.

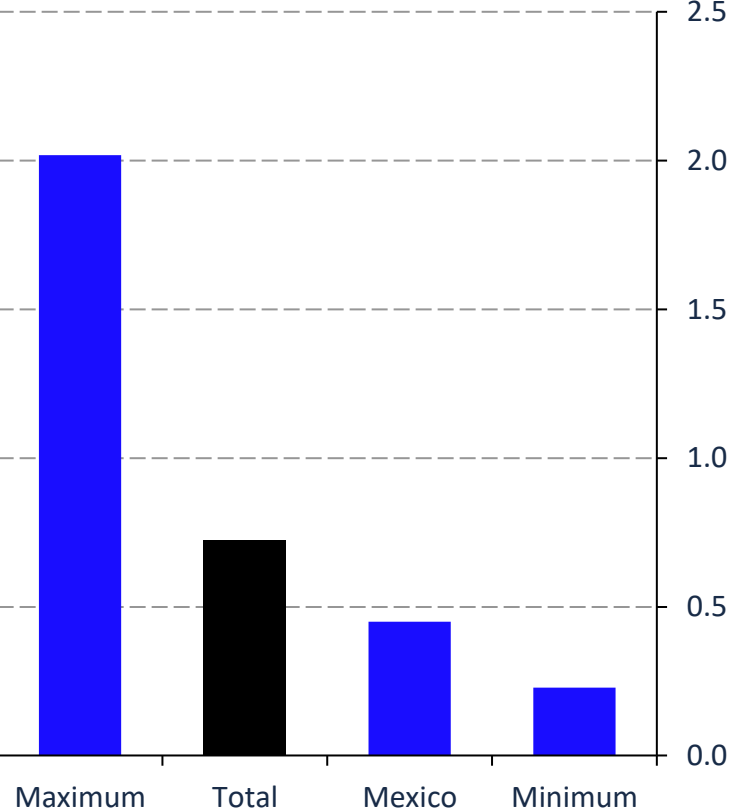
United States: share of total imports by trading partner
% of total imports



China: share of total exports by trading partner
% of total exports



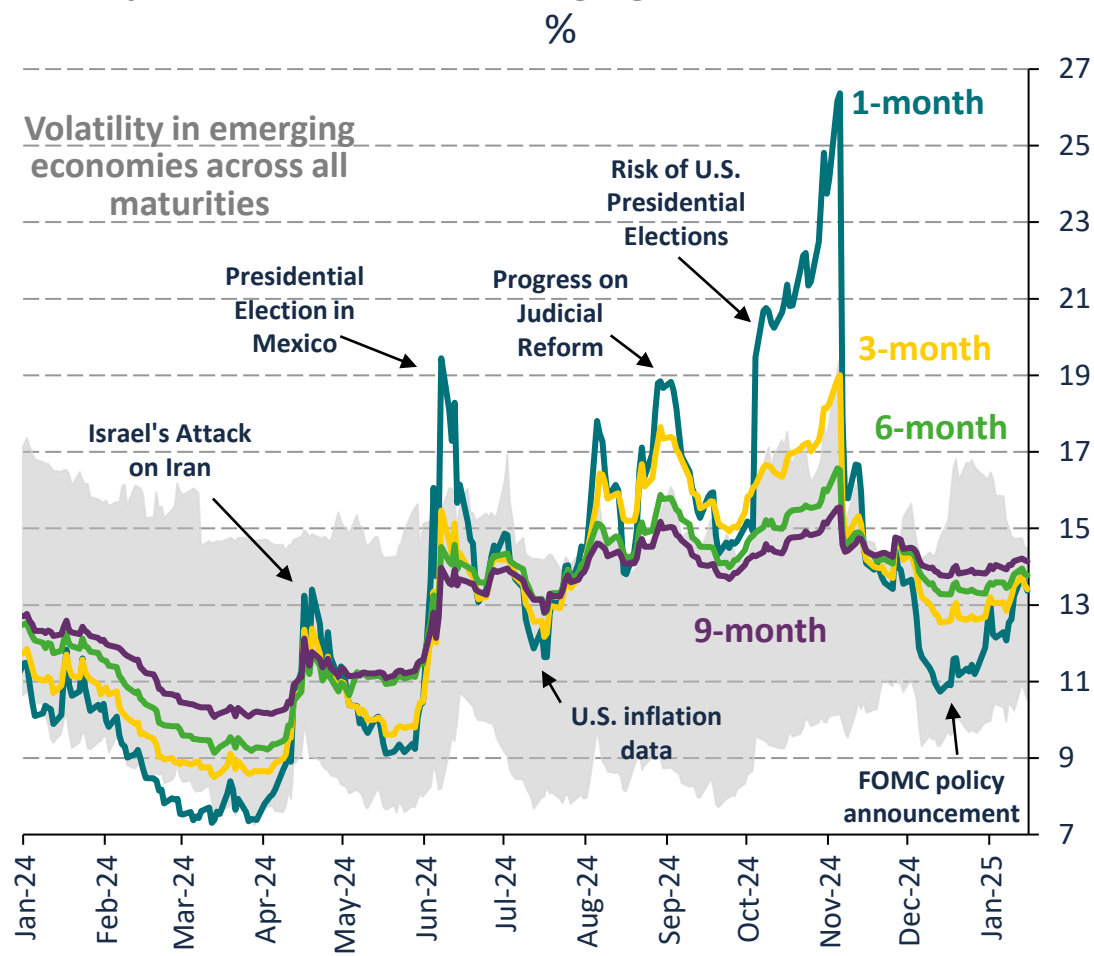
United States: imports deviating from their inertial trend by trading partner in 2023
% of the total import value from each trading partner



Source: Banco de México with data from Trade Data Monitor.

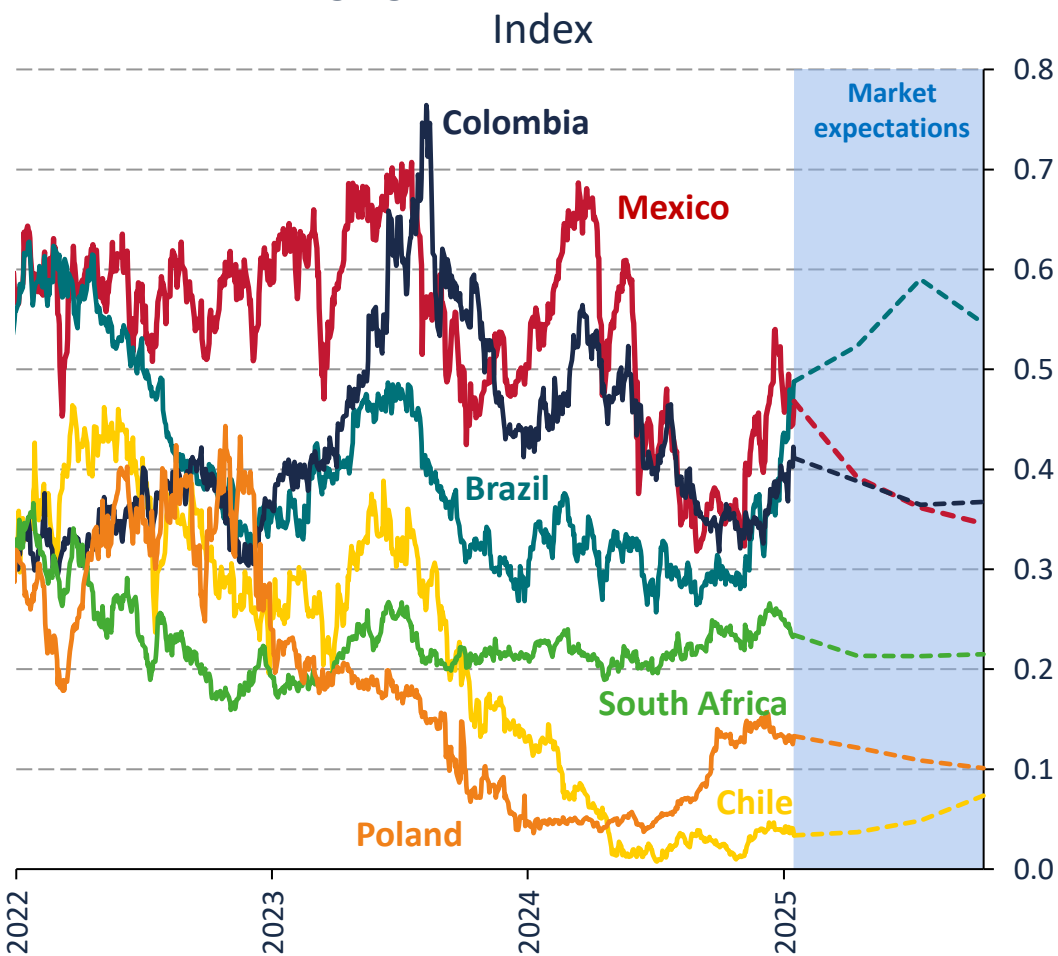
Financial markets in Mexico experienced periods of volatility throughout 2024, where global factors also played an important role.

Implied volatility at different maturities for the Mexican peso and selected emerging market currencies



Note: The emerging countries included are Brazil, Colombia, South Africa, Poland, and Chile.
Source: Bloomberg

Volatility-adjusted spreads between interest rates of emerging markets and of the U.S.



Source: Banco de México with data from Bloomberg.

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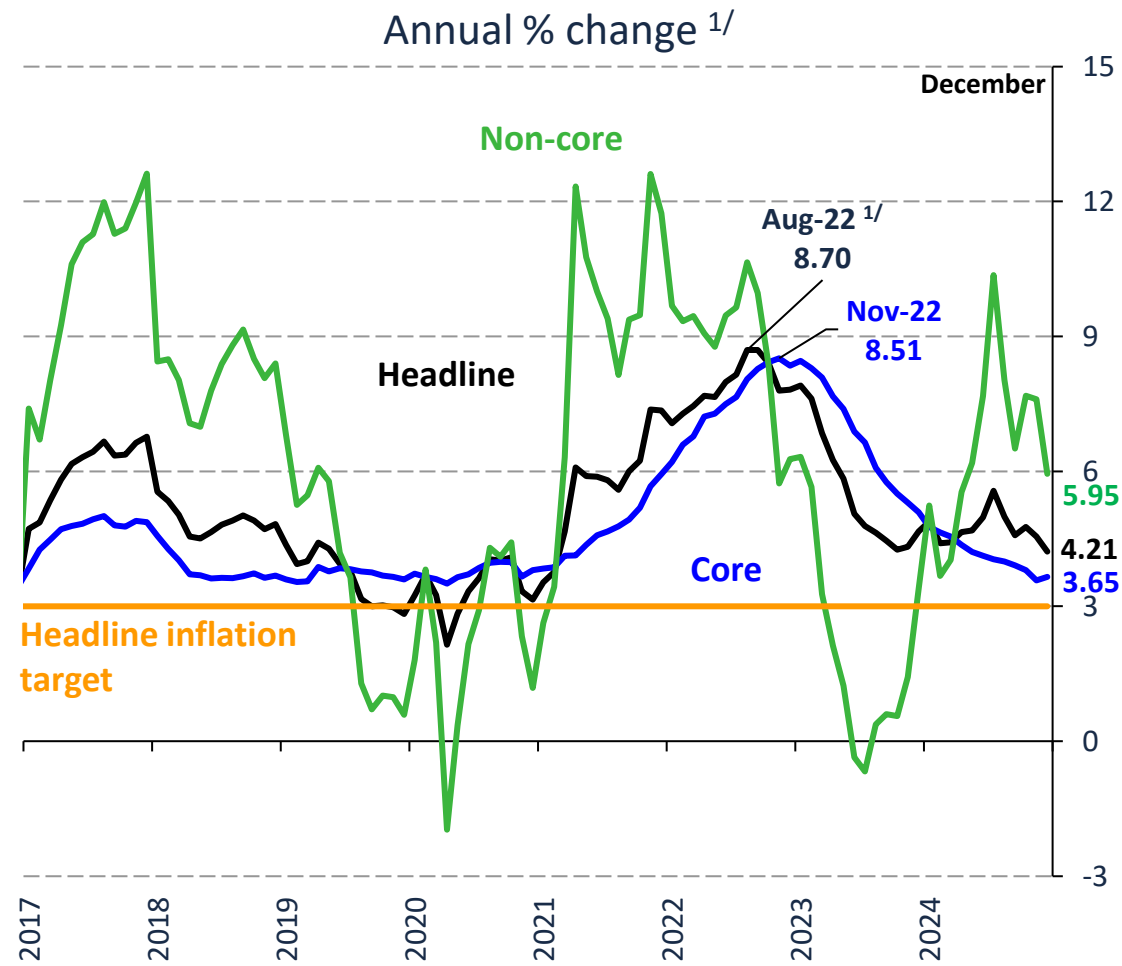
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3 Inflation and its determinants

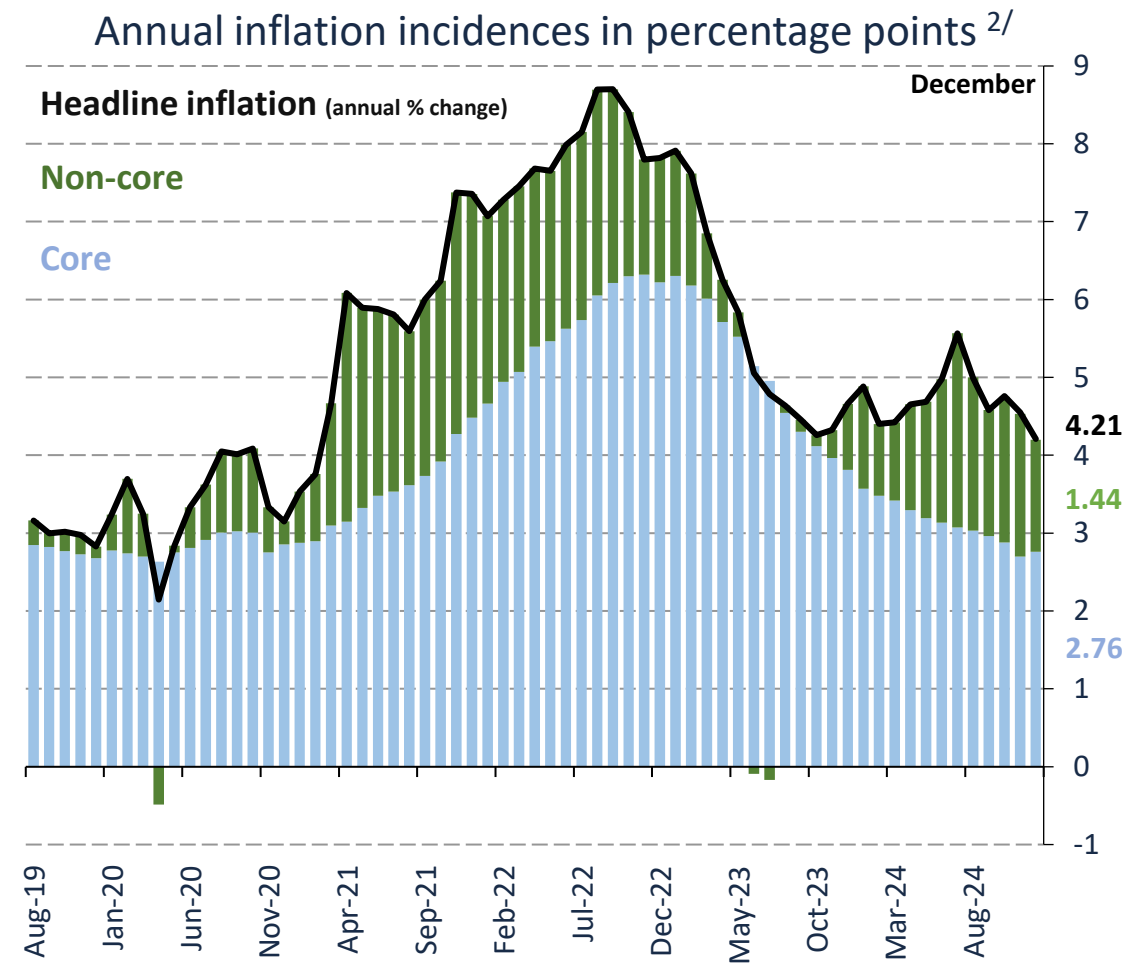
4 Monetary policy

Headline inflation has been affected by supply-side shocks to the non-core component, while core inflation has maintained a downward trend.

Consumer Price Index



^{1/} The headline inflation figure for both August and September 2022 was 8.70%.
Source: Banco de México and INEGI.

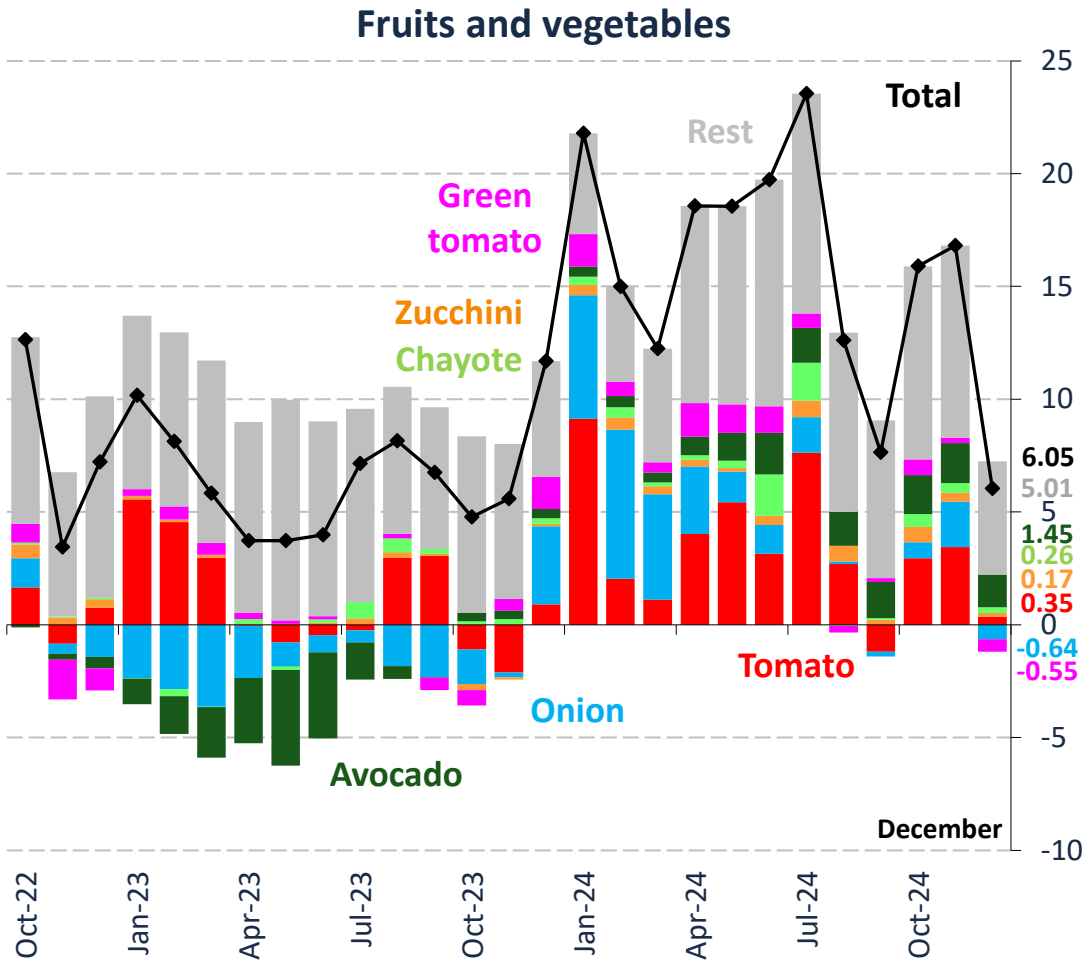
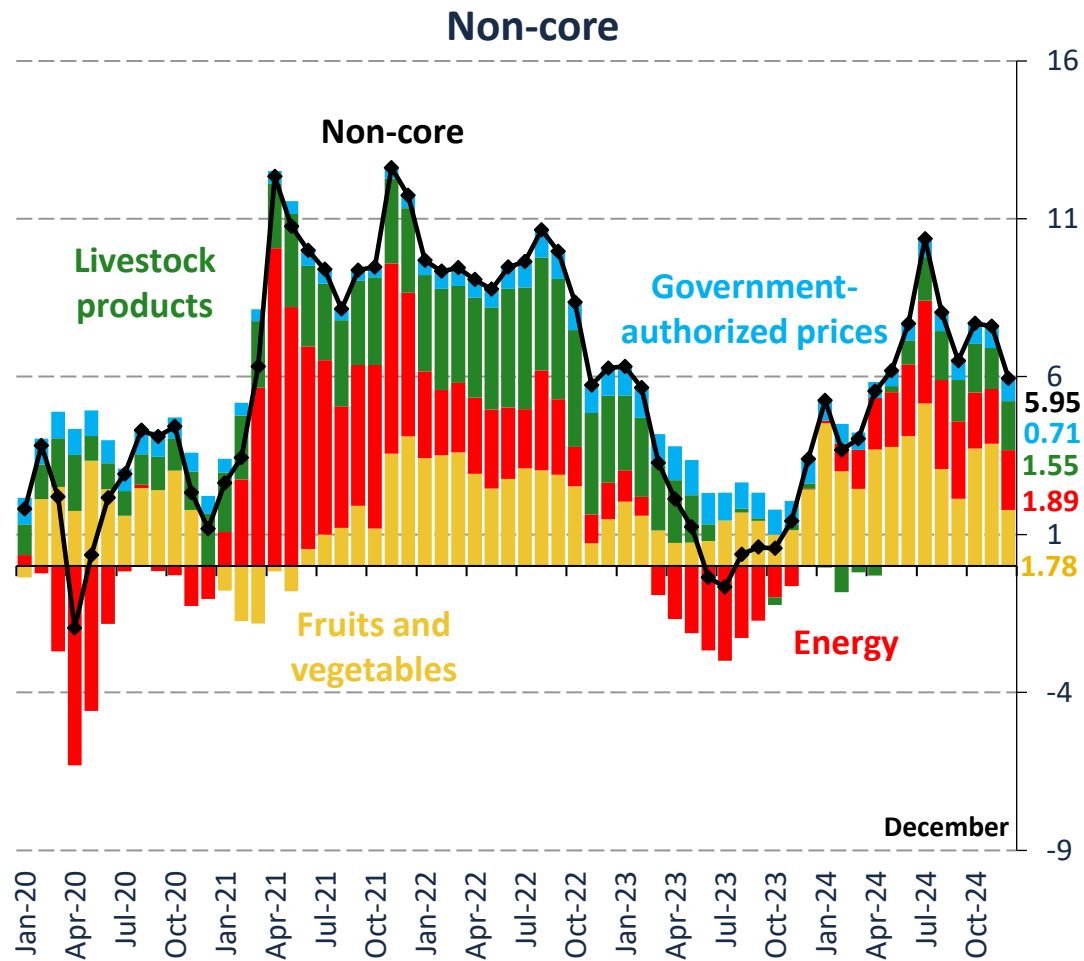


^{2/} The sum of inflation's components may not add up due to rounding.
Source: Prepared by Banco de México with data from INEGI.

Non-core inflation dynamics have been influenced by shocks to certain goods within the agricultural and energy components. In some cases, these shocks have dissipated.

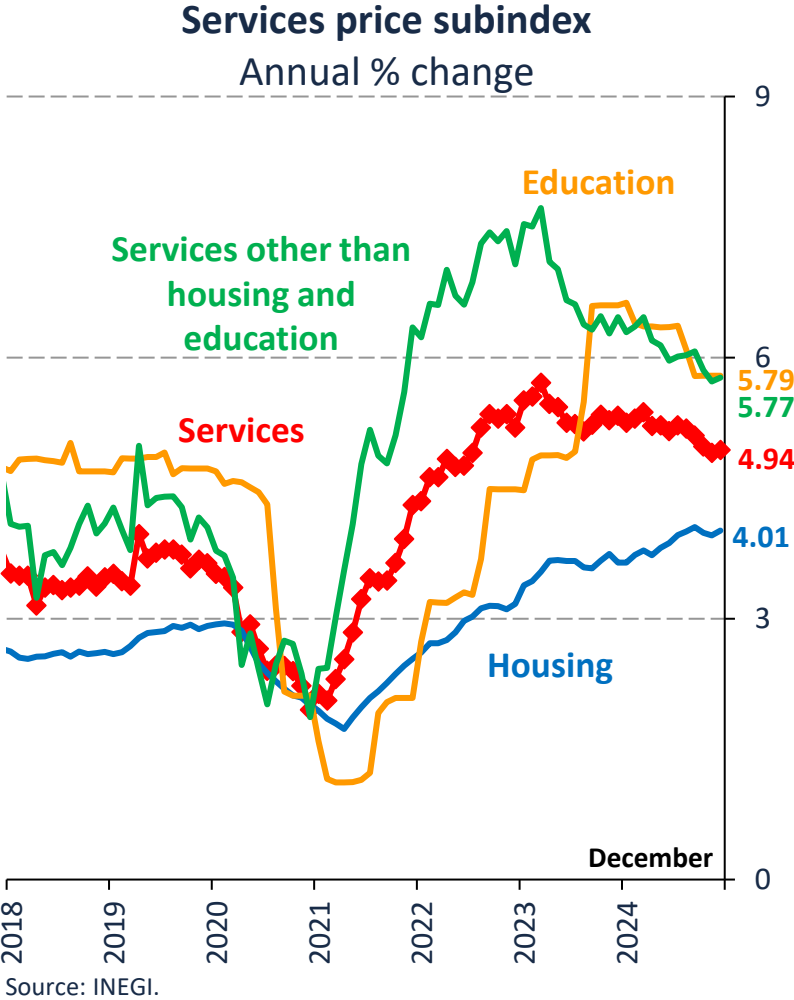
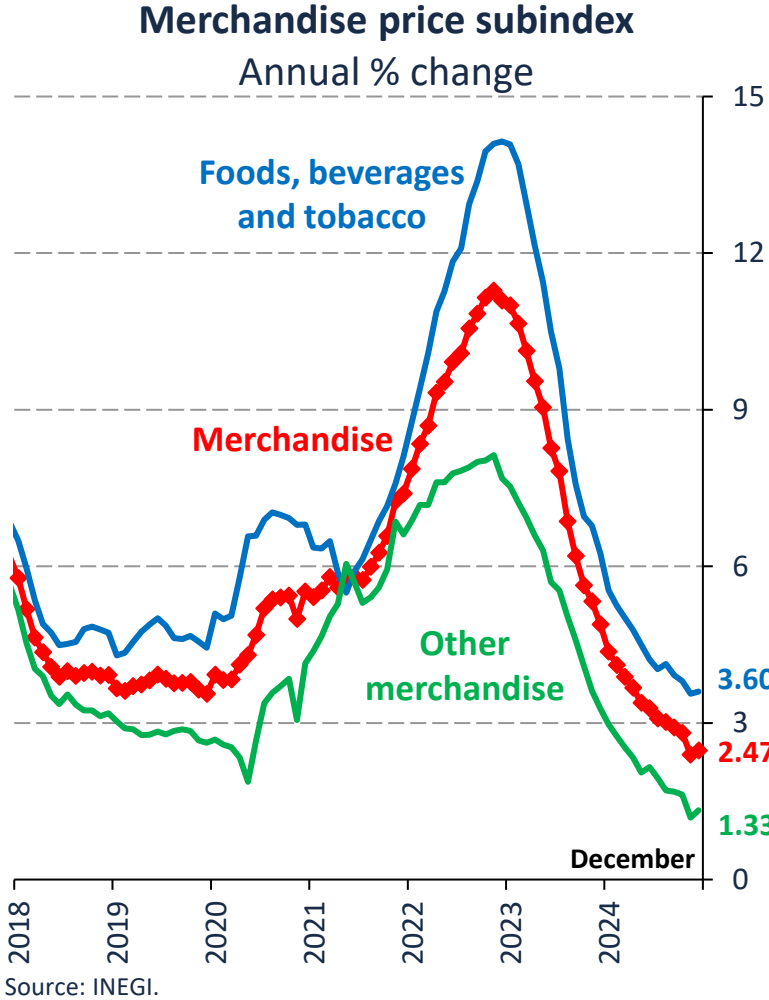
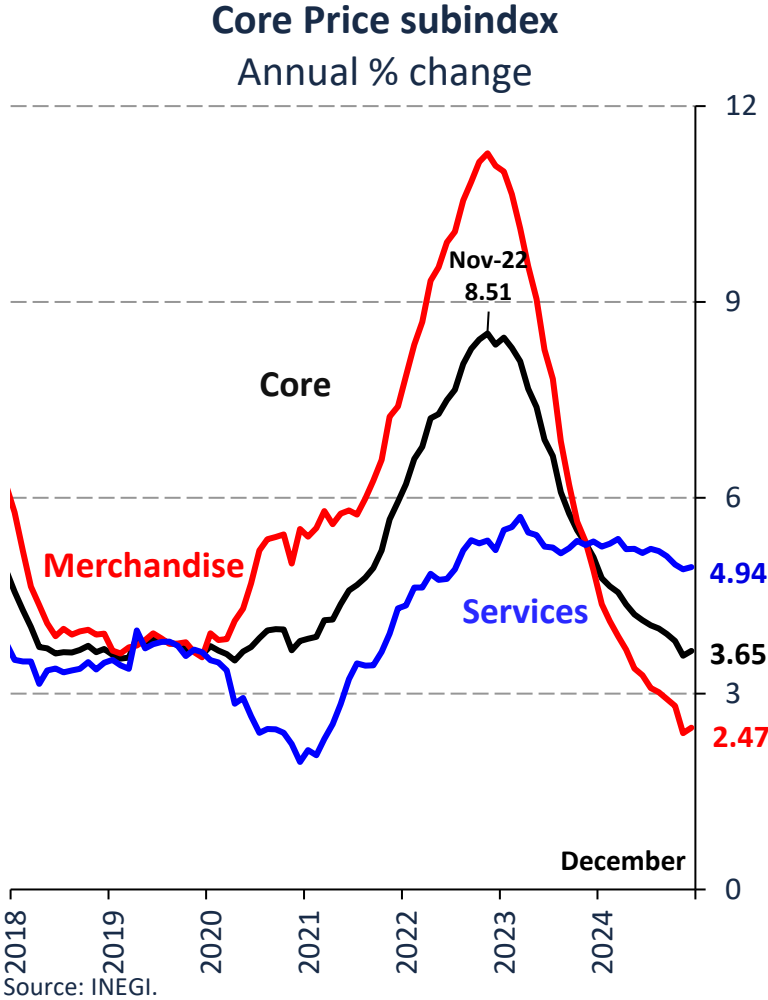
Non-core price index

Annual % change and incidences in percentage points ^{1/}



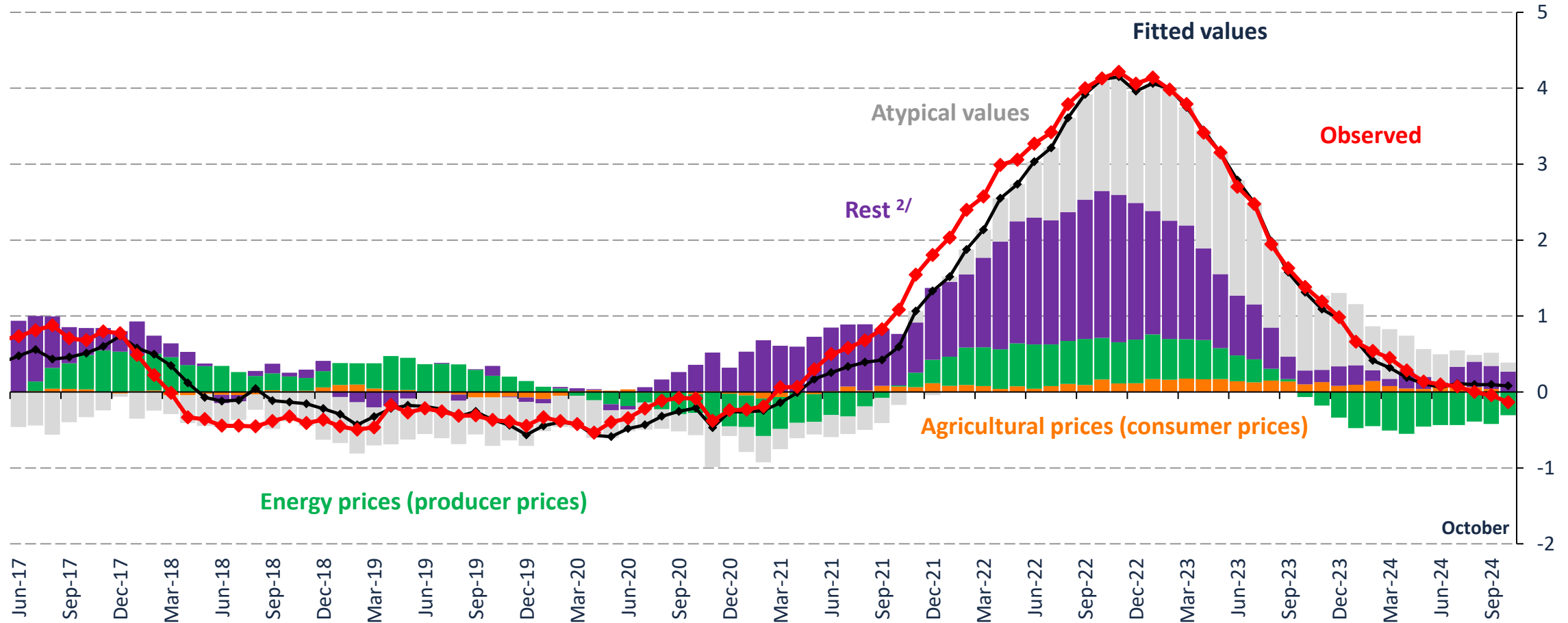
^{1/} The sum of inflation's components may not add up due to rounding.
Source: INEGI.

Within core inflation, the merchandise component maintained its downward trajectory, while the services component has shown persistence, although it has continued to decrease.



Evidence suggests a low pass-through of non-core component prices to core inflation.

Core inflation: Contributions to annual variation by decomposing persistence ^{1/} Deviations from historical average in percent



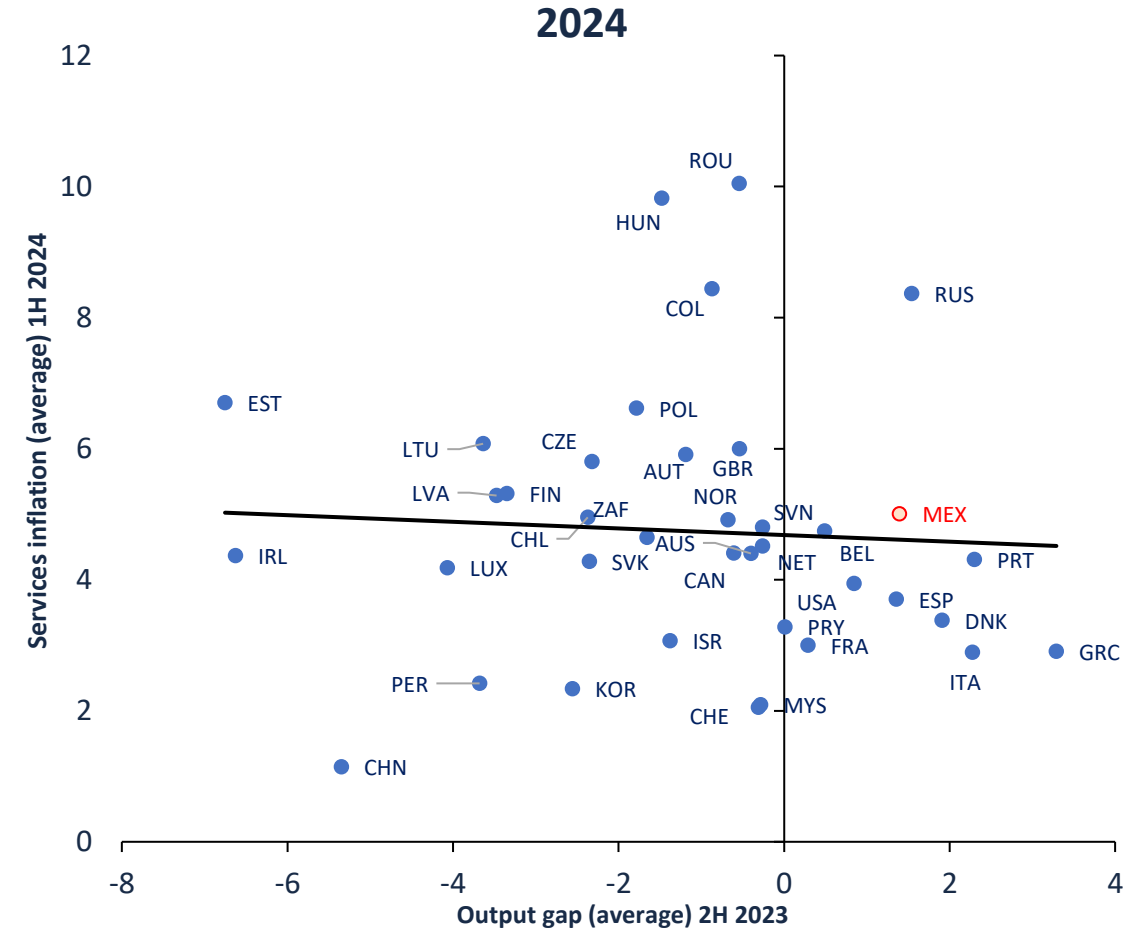
1/ A linear autoregressive model is estimated using the stepwise methodology, i.e., lag order is determined using this methodology (lags significant at 90%). The estimation period starts in 2007 up to most recent data. Contributions to the annual variation are shown as differences with respect to the average historical contributions.

2/ It includes: exchange rate, wages, the CP11 slack indicator from Banco de México, international food and non-food prices, and food and non-food prices from Mexico's consumer price index. Historical deviation refers to the sample from 2007 up to now.

Source: Banco de México with data from INEGI.

Output gap and services inflation

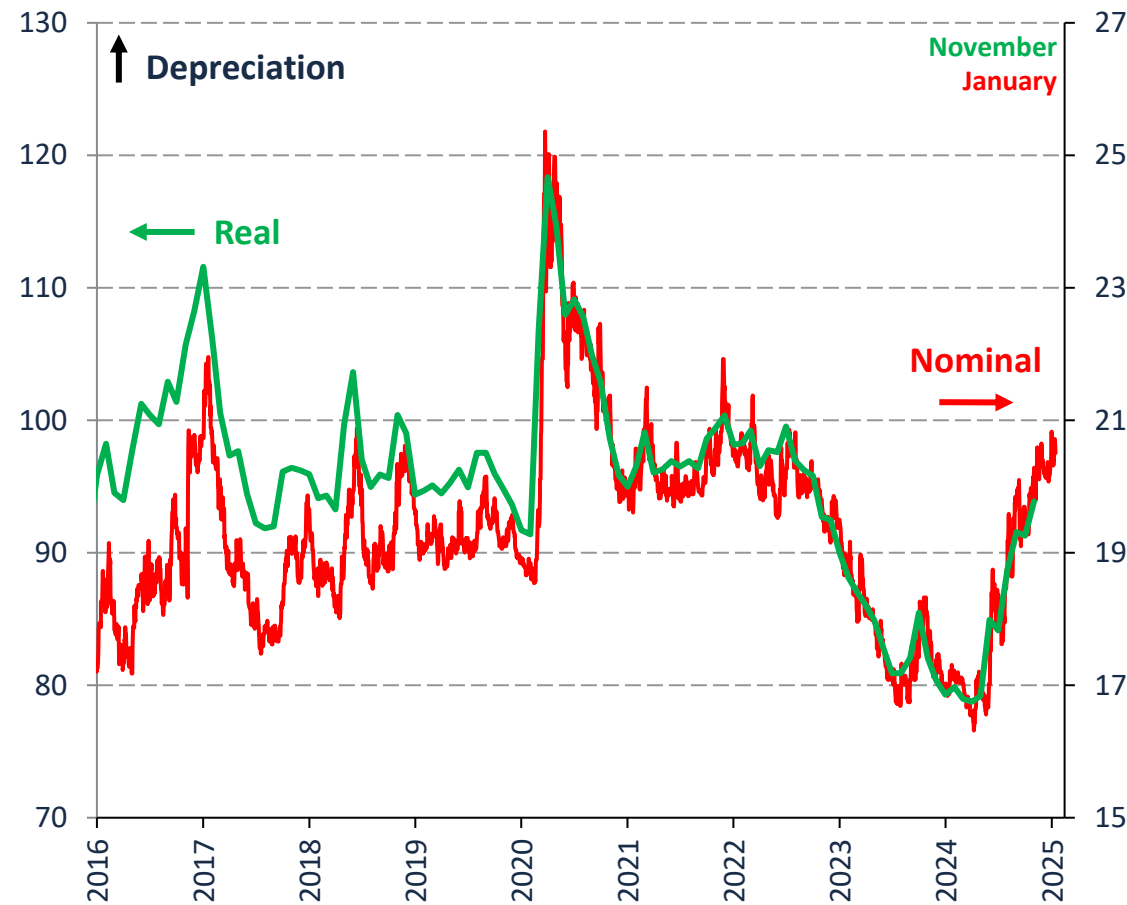
% of potential GDP, %



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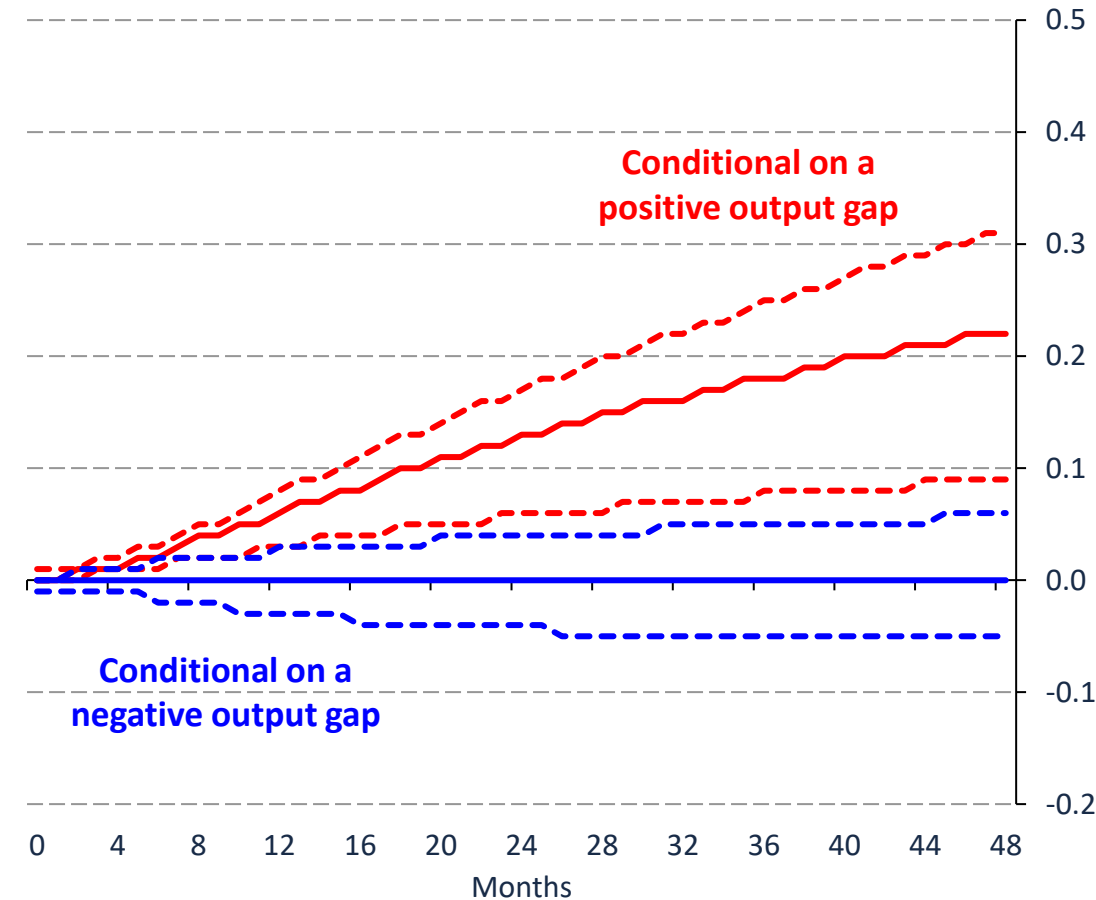
The Mexican peso has depreciated, and new episodes of volatility cannot be ruled out. Still, the country maintains solid fundamentals. Evidence suggests that the exchange rate pass-through is low and tends to be lower under economic slack conditions.

Nominal and real exchange rate
Pesos per USD and index 2016 = 100



Source: Bloomberg.

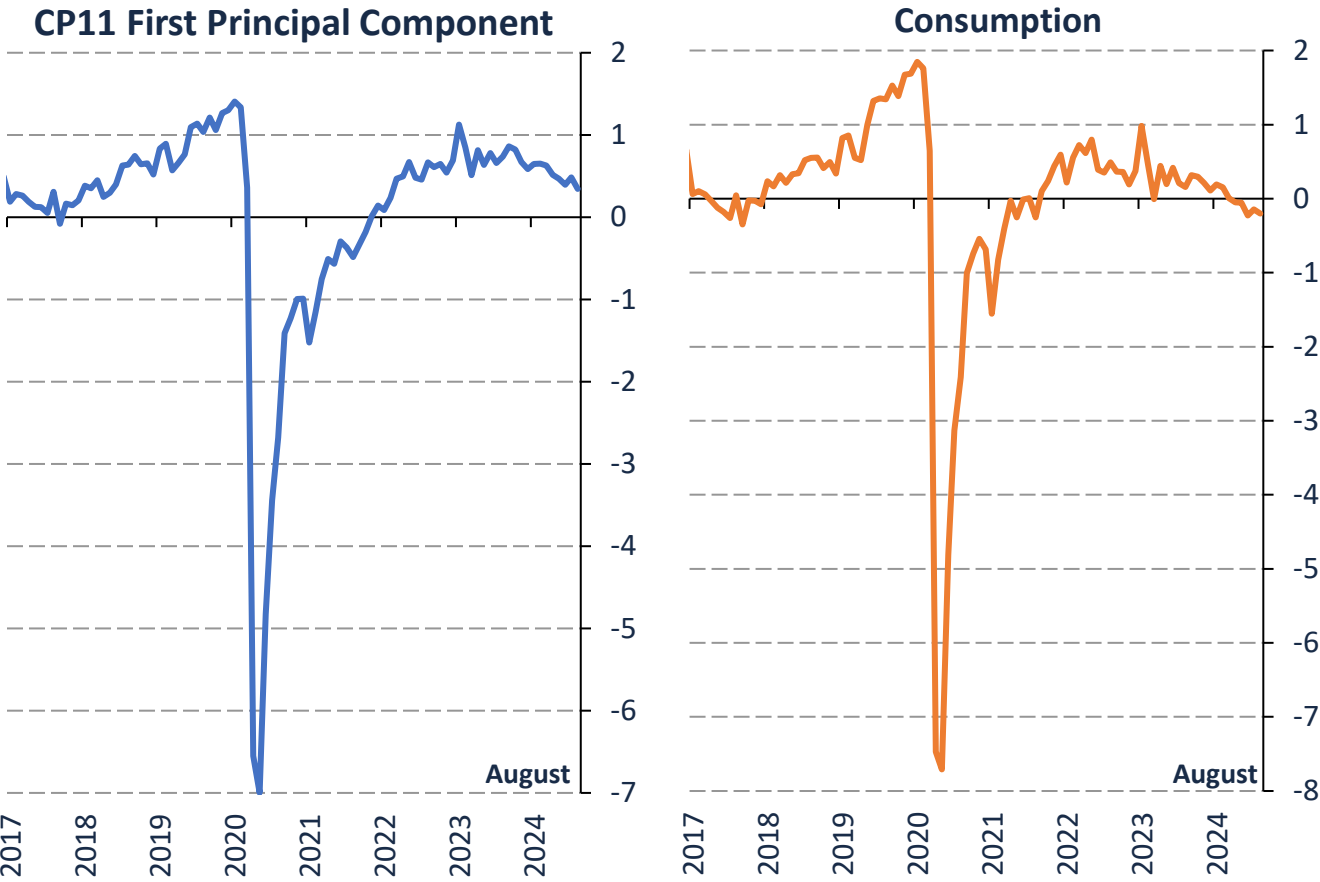
Accumulated pass-through elasticity of the
exchange rate to the headline price level
%



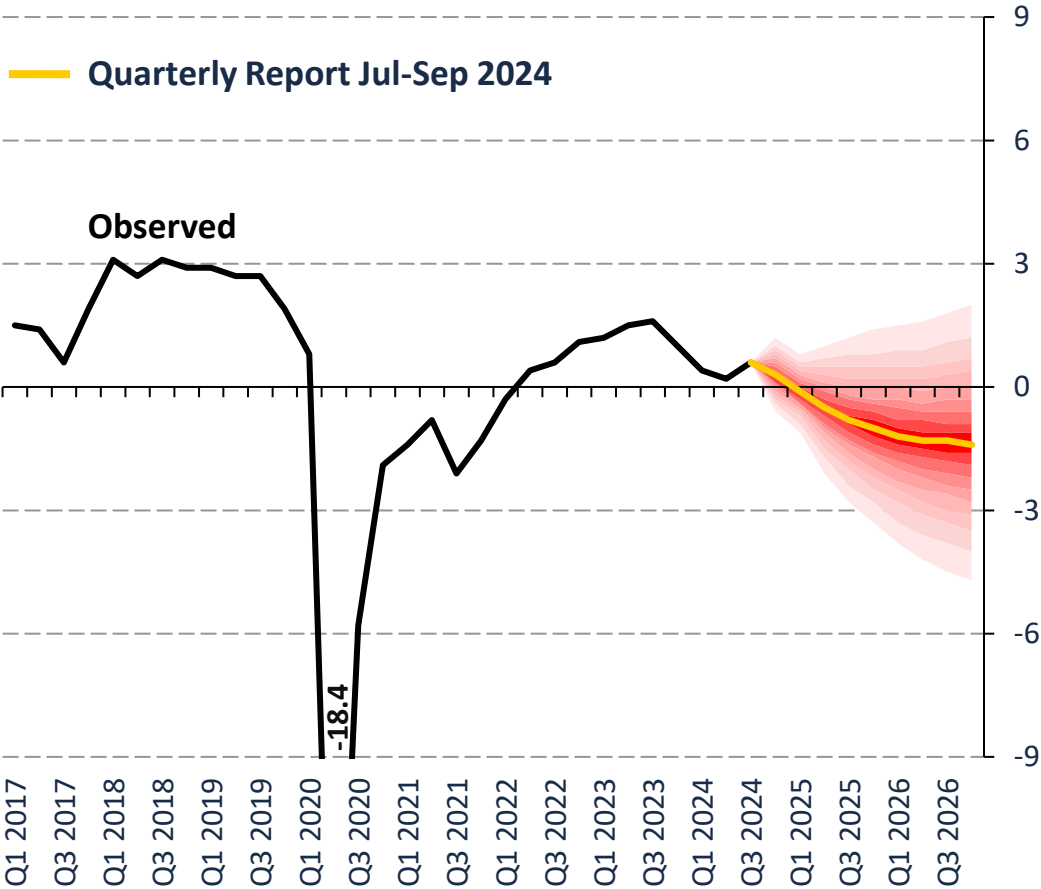
Source: Banco de México's estimation according to a model conditional on the output gap. For more details, see Box 5 of the Quarterly Report April-June 2024.

It is anticipated that the economic slack conditions will continue to ease.

Monthly Slack Indicators ^{1/}



Fan chart: output gap estimate, s. a.
% of potential GDP

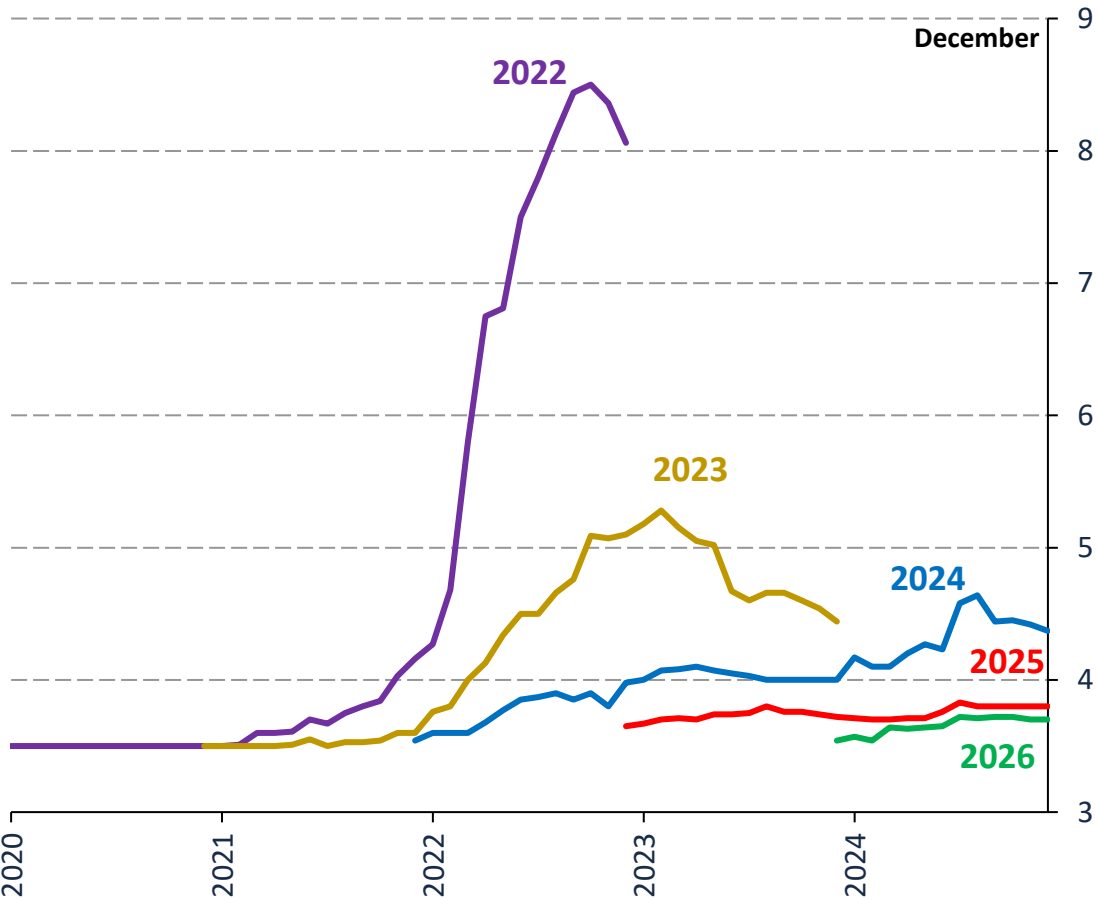


1/ Main Indicators constructed using CCM methodology; see Banco de México (2018), “Quarterly Report, October December 2017”, p.47. Monthly slack indicators are constructed with the main component of a set of series which includes 11 indicators. Slack indicators of consumption is based on the first main component of sets of series which includes 6 indicators. Source: Prepared by Banco de México with data from INEGI and Banco de México.

s. a./ seasonally adjusted figures.
Note: In the present Report the forecast begins in Q4 2024. In the previous Report, it started in Q3 2024. Source: Banco de México.

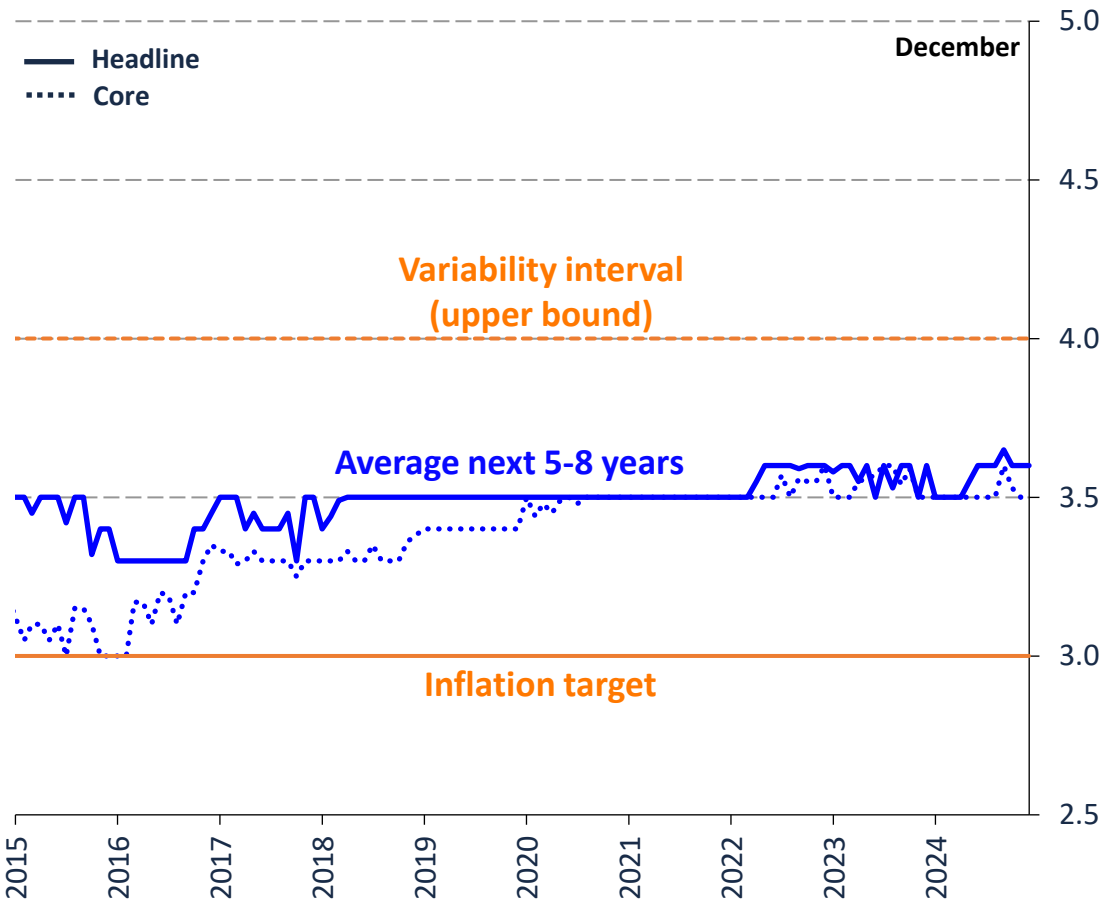
Throughout this inflationary episode, characterized by large-scale shocks, the monetary stance has contributed to preserving longer-term inflation expectations well anchored.

Median of headline inflation expectations at the end of the year
%



Source: Banco de México's Survey of Private Sector Forecasters.

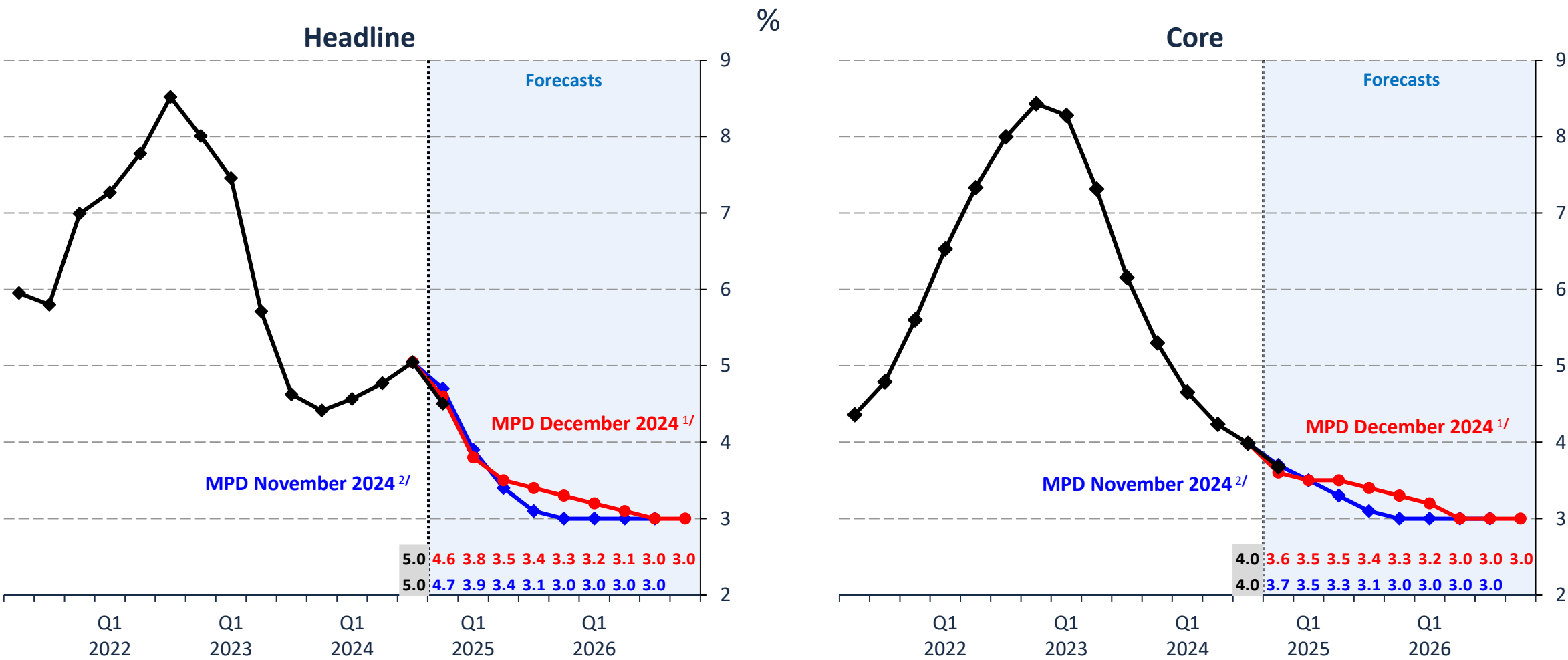
Median of long-term inflation expectations
%



Source: Banco de México's Survey of Private Sector Forecasters.

Headline and core inflation are expected to follow a downward trend.

Annual inflation forecasts ^{1/}



Note: MPD refers to Monetary Policy Decision. 1/ Forecast since December 2024. It corresponds to the forecast published in the Monetary Policy Statement of December 19, 2024. 2/ Forecast since November 2024. It corresponds to the forecast published in the Monetary Policy Statement of November 14, 2024. Source: INEGI for annual variation observed data and Banco de México for forecasts.

Outline

1

External conditions

2

Current situation of the Mexican economy

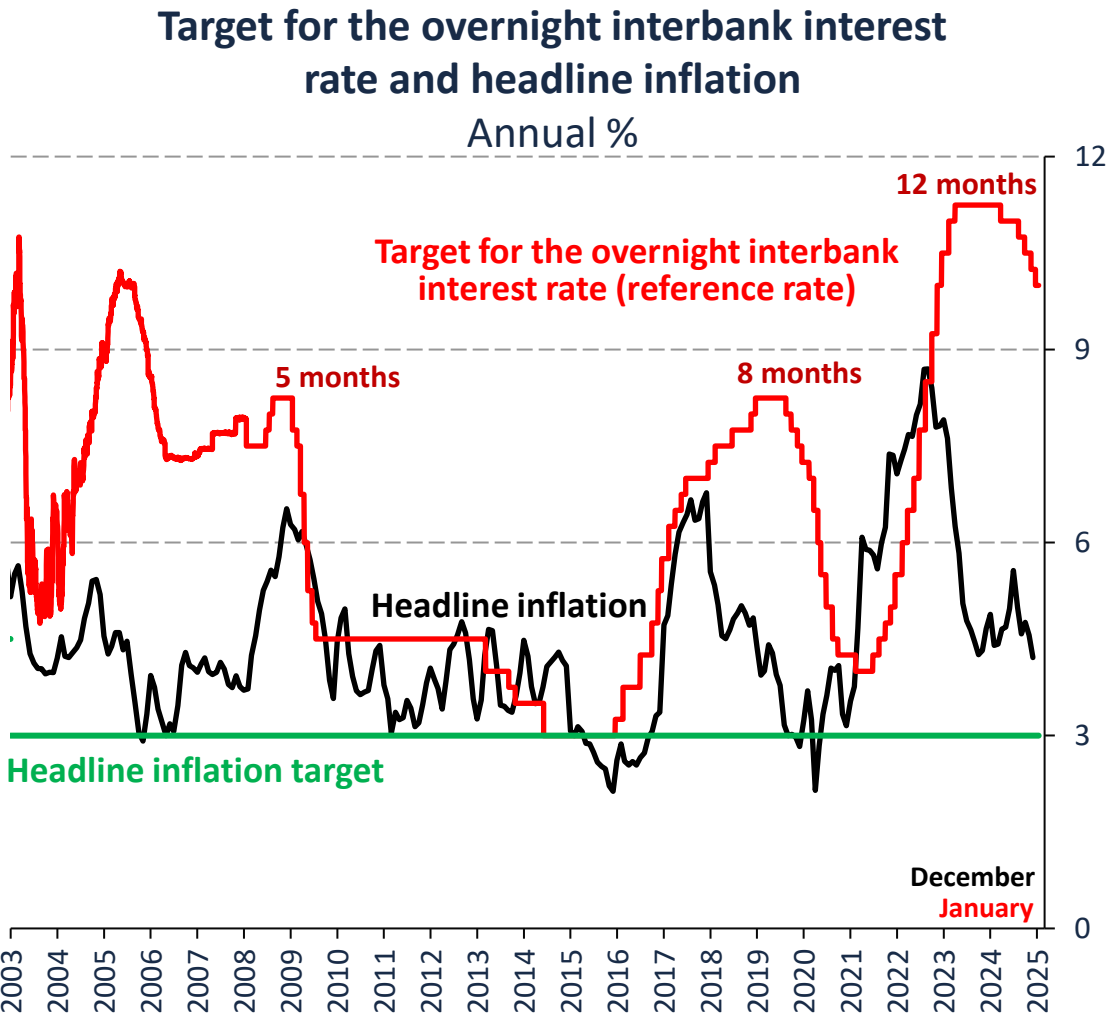
3

Inflation and its determinants

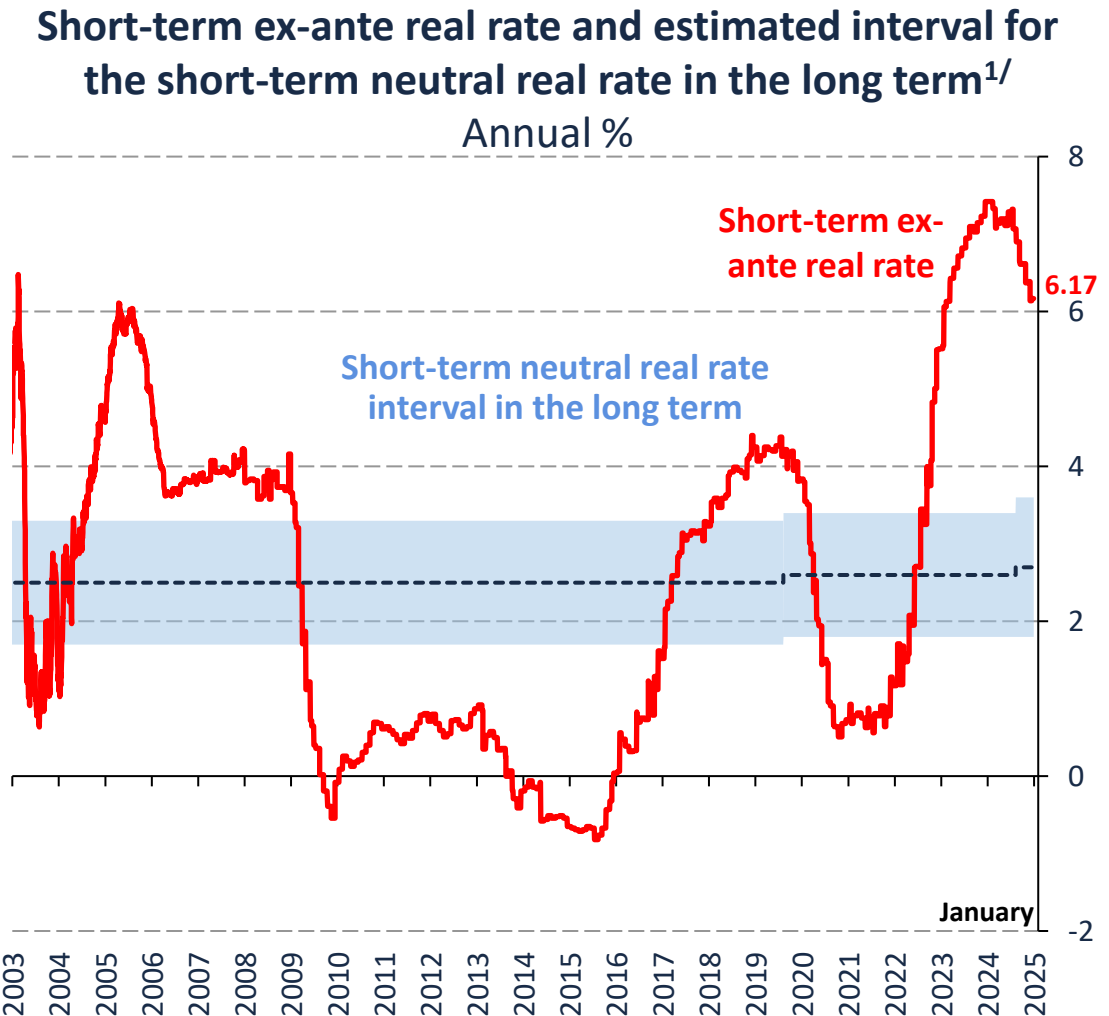
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Monetary policy

In 2024, the Board of Governors decided to lower the reference rate by 125 bps to 10%. Monetary policy stance remains clearly restrictive.

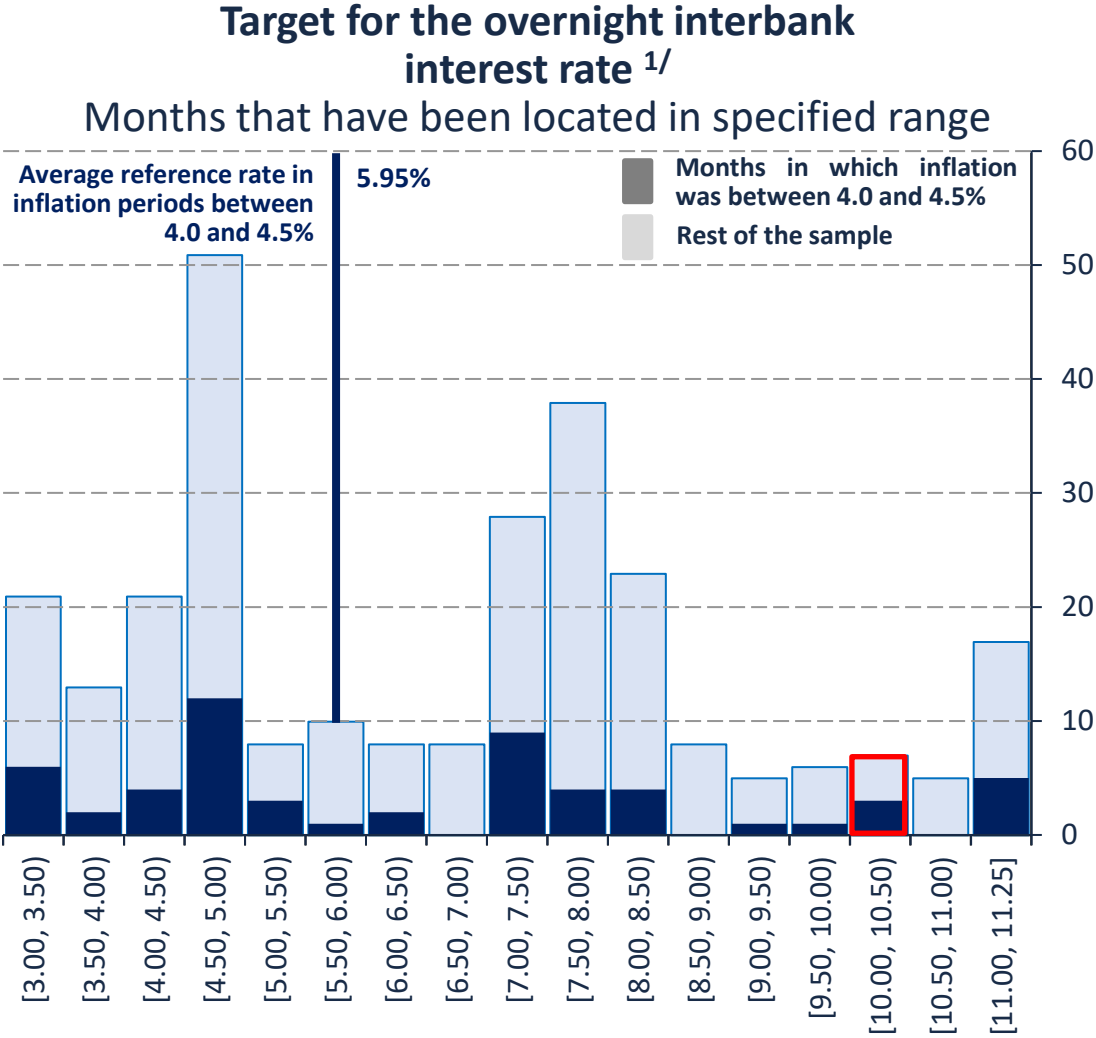


Source: Banco de México and INEGI.

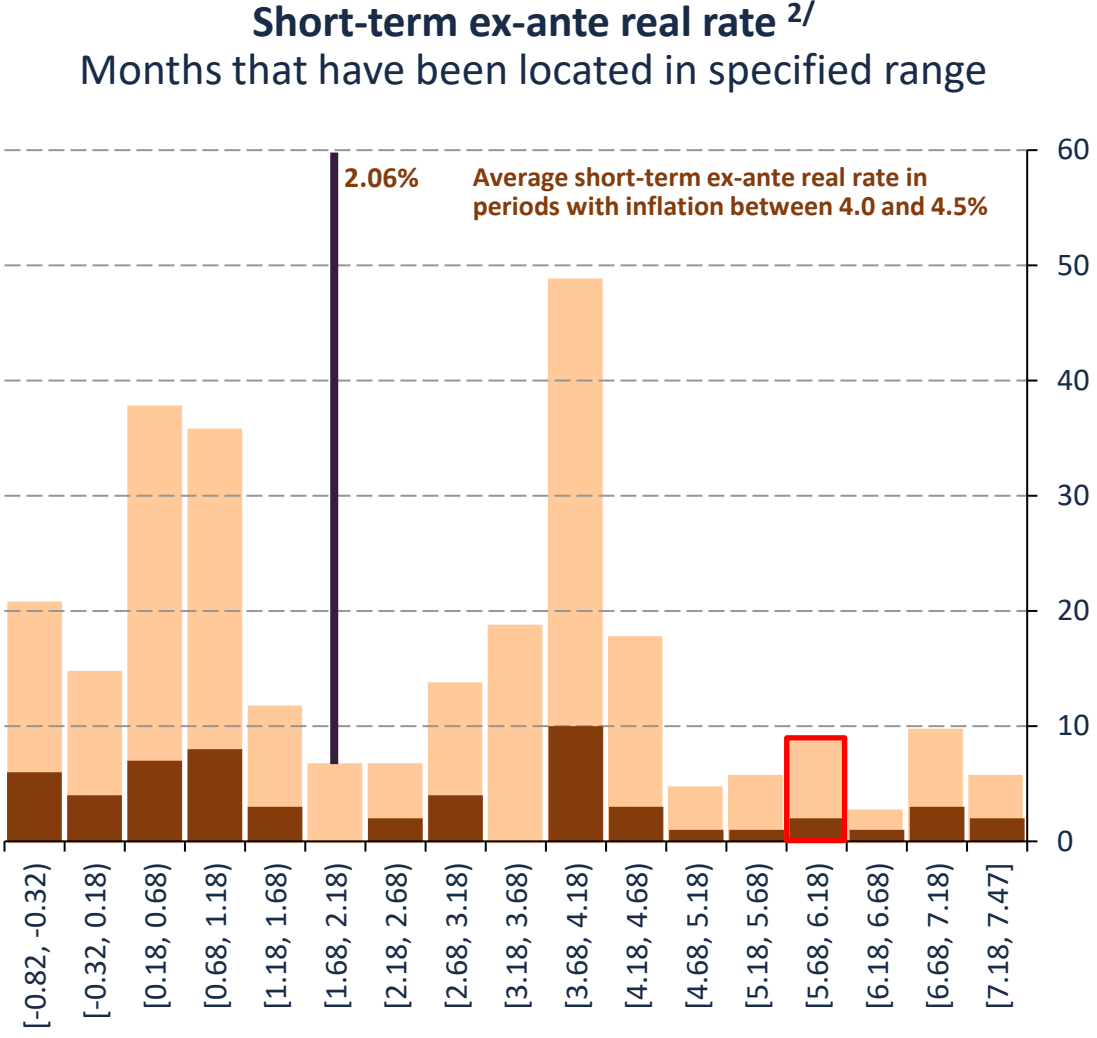


1/ The short-term ex-ante real rate is constructed using the target for the overnight Interbank interest rate and the mean of 12-month inflation expectations drawn from Banco de México's Survey of Private Sector Forecasters. The dotted line corresponds to the midpoint of the interval for the short-term neutral real rate in the long term, which is now between 1.8 and 3.6%. The shaded area corresponds to the estimated interval for the short-term neutral rate in the long term. Source: Banco de México.

The nominal and real ex-ante interest rates remain highly restrictive, compared to other periods in which inflation has been between 4.0 and 4.5%.



1/ The data sample begins in December 2001. Before January 20, 2008, we use the 1-day interbank interest rate.
Source: Banco de México.

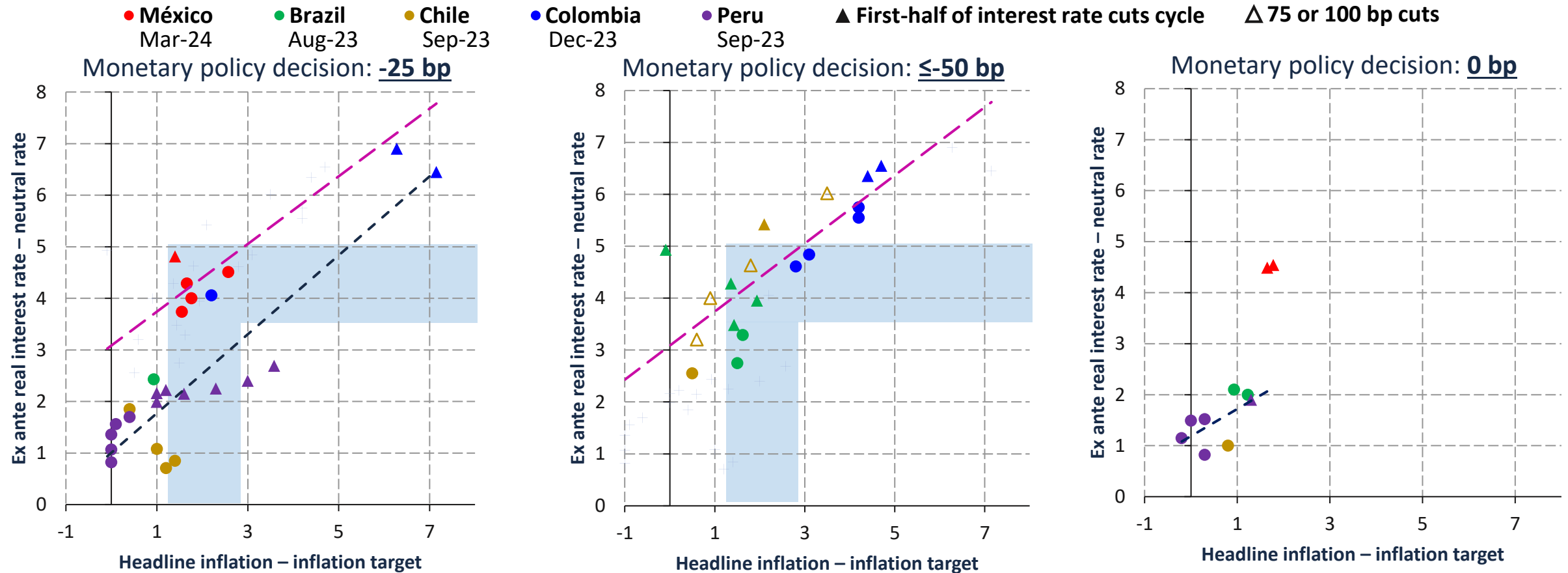


2/ The short-term ex ante real rate is constructed using the target for the overnight Interbank interest rate and the mean of 12-month inflation expectations drawn from Banco de México's Survey of Private Sector Forecasters.
Source: Banco de México.

Banco de México has implemented 25bp policy rate-cuts with an inflation gap close to 2 percentage points and a real ex-ante interest rate gap between 4% and 5%. However, other central banks in the region have implemented larger cuts with similar conditions.

Latin America: inflation and real ex ante interest rate gaps

Percentage points



Note: The 12-month inflation expectations for the real ex-ante interest rate are estimated using the inflation expectations from each central bank or, when unavailable, from the Bloomberg survey.

Source: Banco de México with data from Bloomberg, central banks' web pages, Haver analytics, and INEGI.



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