

Quarterly Report

October - December 2023

February 28, 2024



BANCO DE MÉXICO®

Characterization of the period covered by this Report

Externally

- **Moderation** of world economic activity.
- **Advances** in the **disinflation process worldwide**.
- **Financial and monetary conditions** remain **tight**.

Domestically

- **Moderation** of economic activity in **Q4 2023**, although most of the year showed resilience.
- **Headline inflation** is significantly **below the highest records** of this episode, but still **above target**.
- **Core inflation** continues **decreasing**, but still **remains at relatively high levels**.

Monetary policy

- The Governing Board **left the reference rate unchanged at 11.25%**.
- Throughout this inflationary period, Banco de México **has reaffirmed**, through its actions and communication, its firm **commitment** to achieving its **price stability mandate**.

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2 Current situation of the Mexican economy

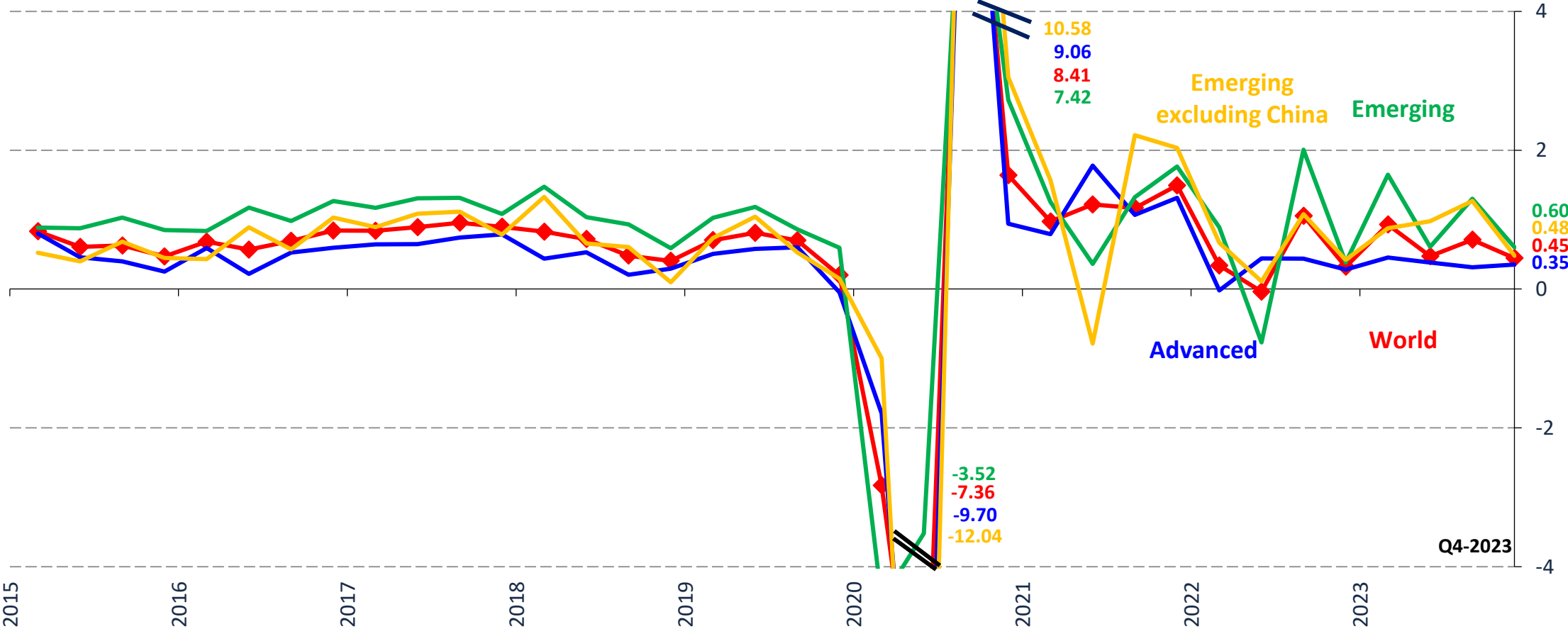
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In Q4-2023, world economic activity is anticipated to have expanded at a more moderate rate than in the previous quarter, although it remains resilient.

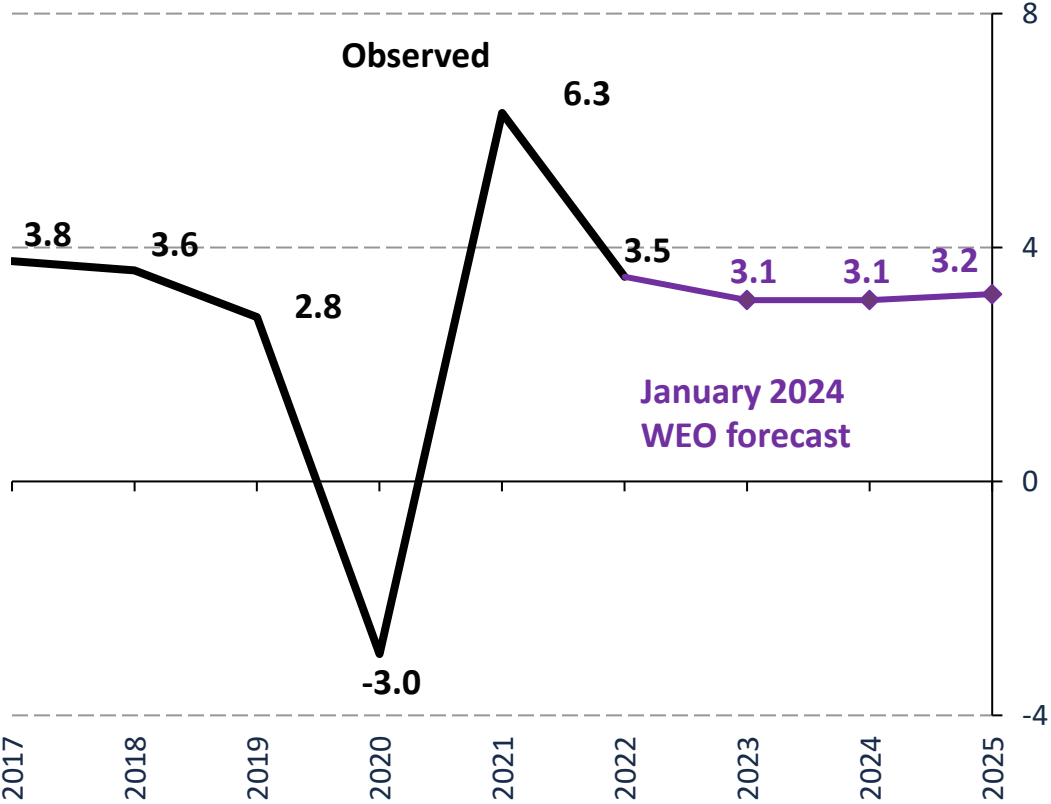
Real GDP Growth Quarterly % change, s. a.



s. a. / Seasonally adjusted figures.
 Note: The sample of countries used for the calculation represents 85.4% of world GDP adjusted for purchasing power parity. Forecasts are used for some countries in the sample for Q4-2023. Updated with information available as of February 26, 2024.
 Source: Prepared by Banco de México with information from Haver Analytics and J.P. Morgan.

The pace of expansion of world economic activity in 2024 is expected to be similar to that of 2023. However, the change between years in each country's growth rate is anticipated to be heterogeneous.

World GDP growth forecast
Annual % change



GDP growth forecast

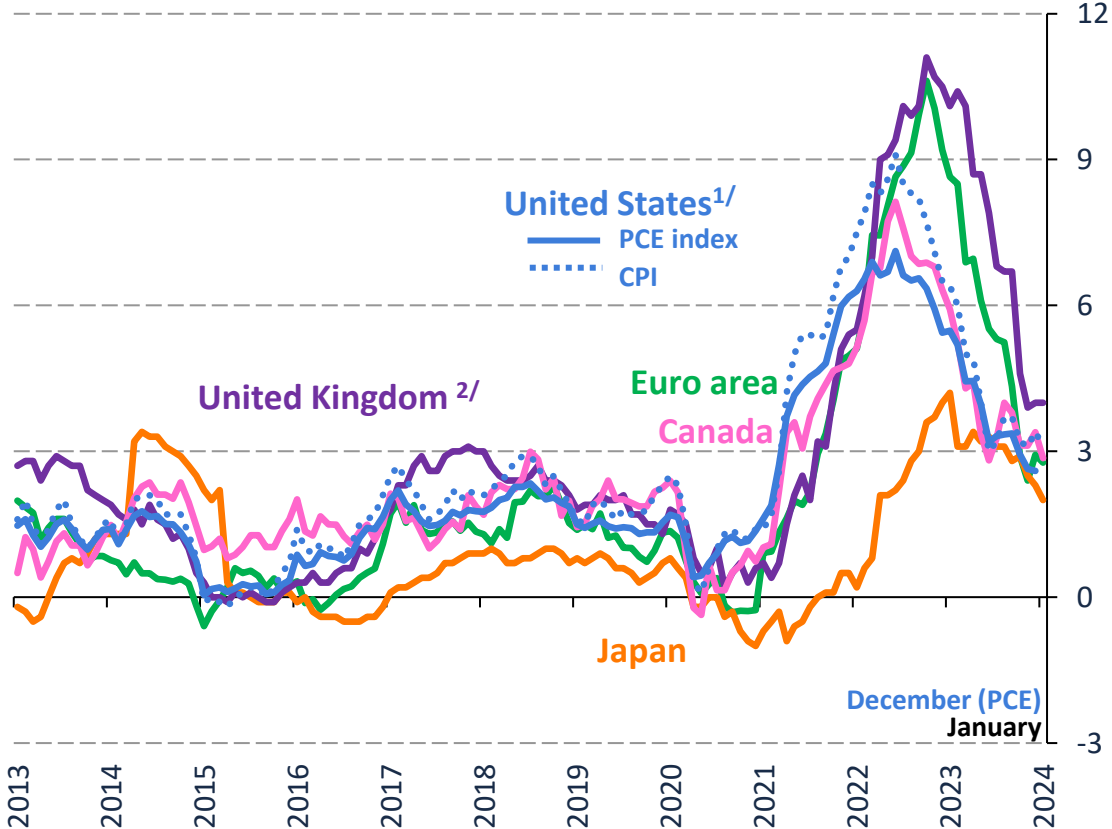
	WEO January 2024 Annual % Change			Change from WEO October 2023 Percentage Points		
	2023	2024	2025	2023	2024	2025
World	3.1	3.1	3.2	0.1	0.2	0.0
Advanced	1.6	1.5	1.8	0.1	0.1	0.0
United States	2.5	2.1	1.7	0.4	0.6	-0.1
Euro area	0.5	0.9	1.7	-0.2	-0.3	-0.1
Japan	1.9	0.9	0.8	-0.1	-0.1	0.2
United Kingdom	0.5	0.6	1.6	0.0	0.0	-0.4
Emerging	4.1	4.1	4.2	0.1	0.1	0.1
Excl. China	3.6	3.9	4.2	0.1	0.0	0.1
Mexico	3.4	2.7	1.5	0.2	0.6	0.0
China	5.2	4.6	4.1	0.2	0.4	0.0
India	6.7	6.5	6.5	0.4	0.2	0.2
Brazil	3.1	1.7	1.9	0.0	0.2	0.0

Note: Data for 2023 correspond to estimates from the International Monetary Fund in the World Economic Outlook January 2024.
Source: International Monetary Fund (IMF), World Economic Outlook October 2023 and January 2024.

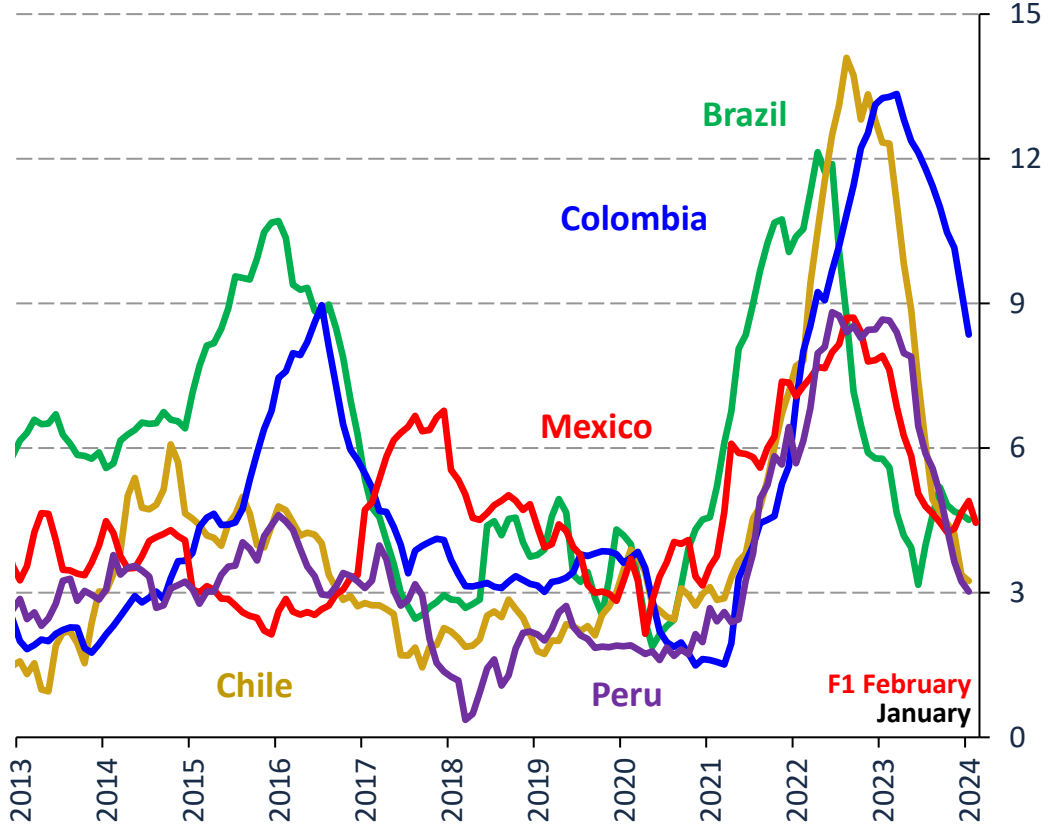
During the period covered by this Report, annual headline inflation declined in most major advanced and emerging economies. However, towards the end of the year, some economies experienced rebounds in inflation that partially or fully reversed in early 2024.

Headline price index Annual % change

Advanced economies



Emerging economies in Latin America



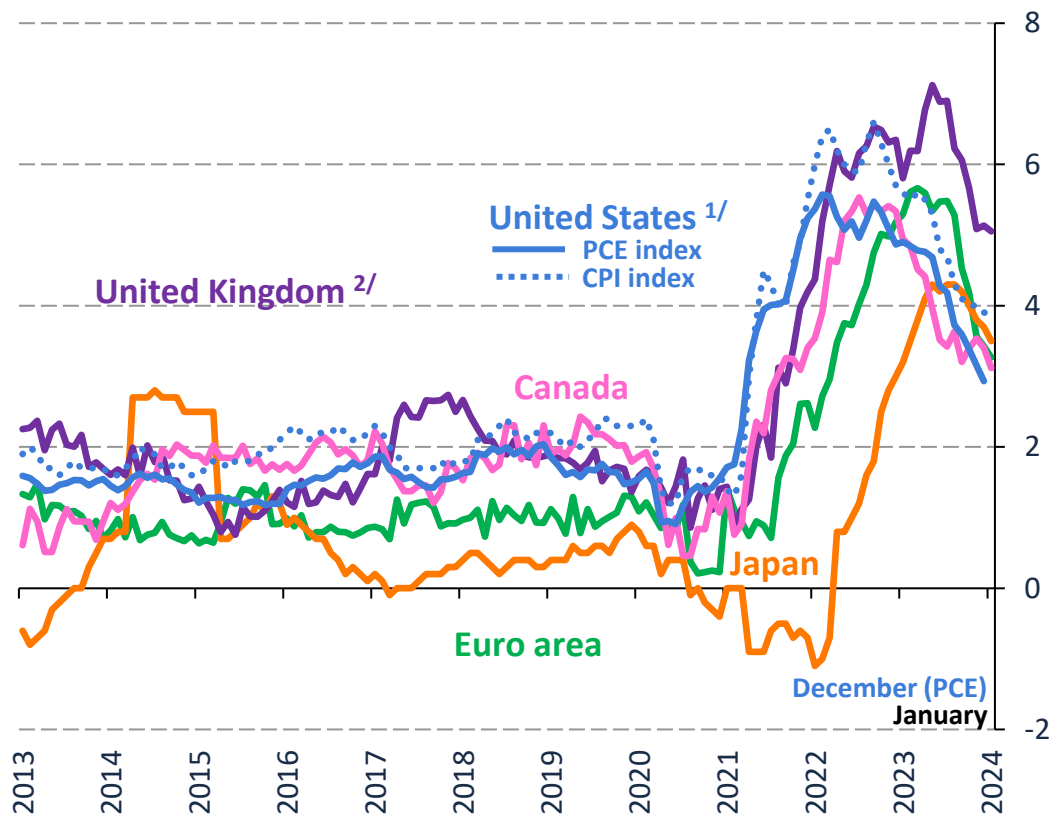
1/ The solid line refers to the Personal Consumption Expenditure Price Index (PCE) and the dotted line shows the Consumer Price Index (CPI). 2/ The harmonized index is used.
Source: Bureau of Economic Analysis, Bureau of Labor Statistics, Eurostat, Bank of Japan, Office for National Statistics of the UK and Statistics Canada.

Source: INEGI and corresponding national statistics offices.

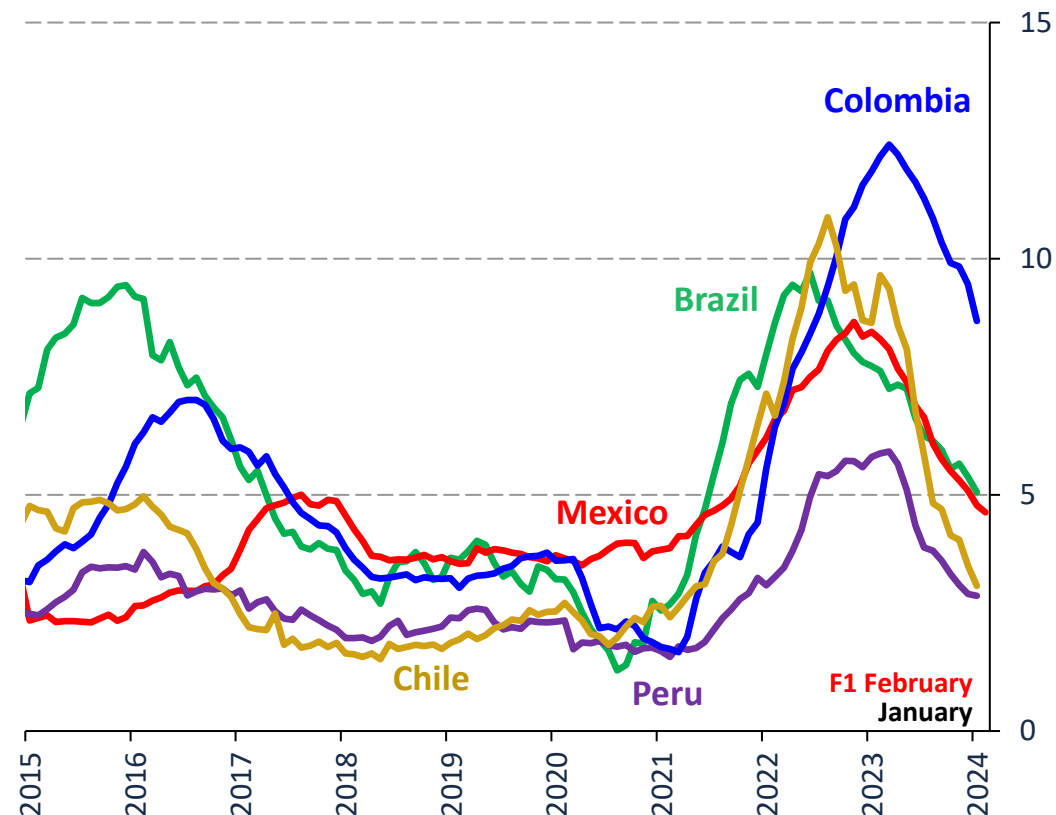
Core inflation continued decreasing. This reflected, to a greater extent, a decline in merchandise inflation, while services inflation has shown some persistence.

Core price index Annual % change

Advanced economies



Emerging economies in Latin America

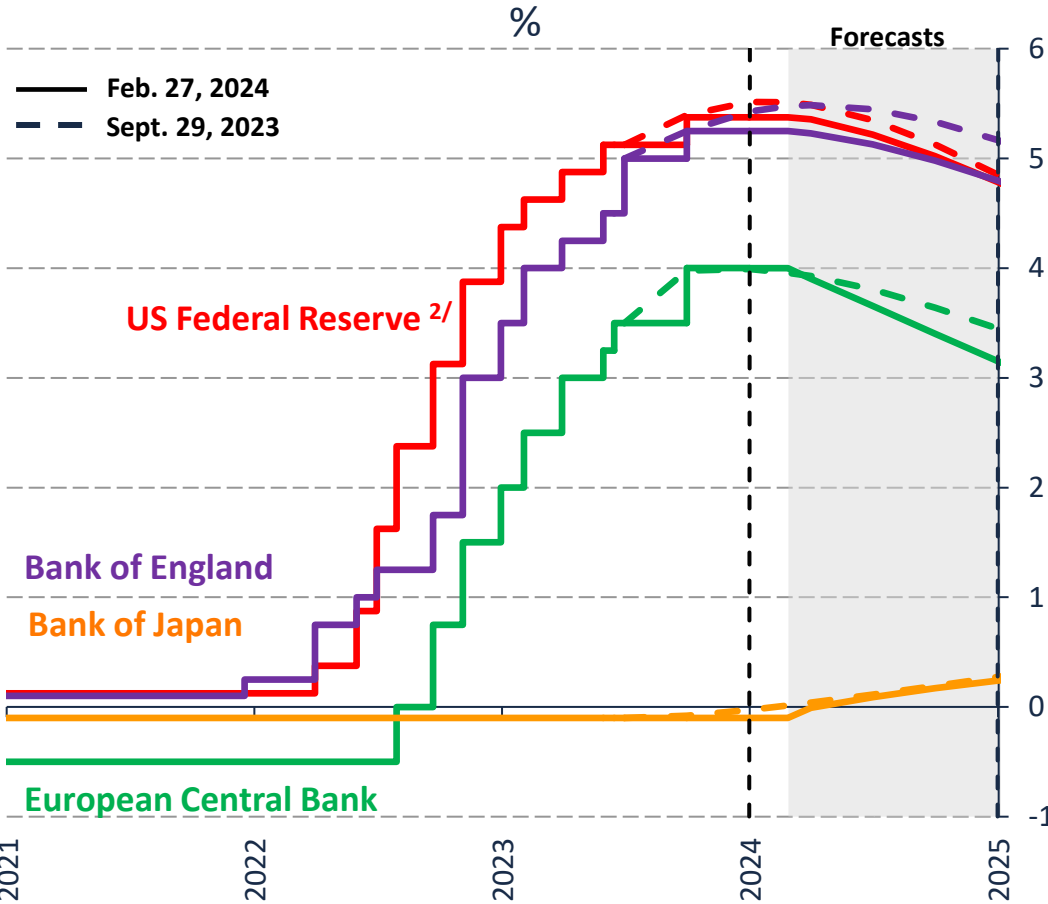


1/ The solid line refers to the Personal Consumption Expenditure Price Index (PCE) and the dotted line shows the Consumer Price Index (CPI). 2/ The harmonized index is used.
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Source: INEGI and corresponding national statistics offices.

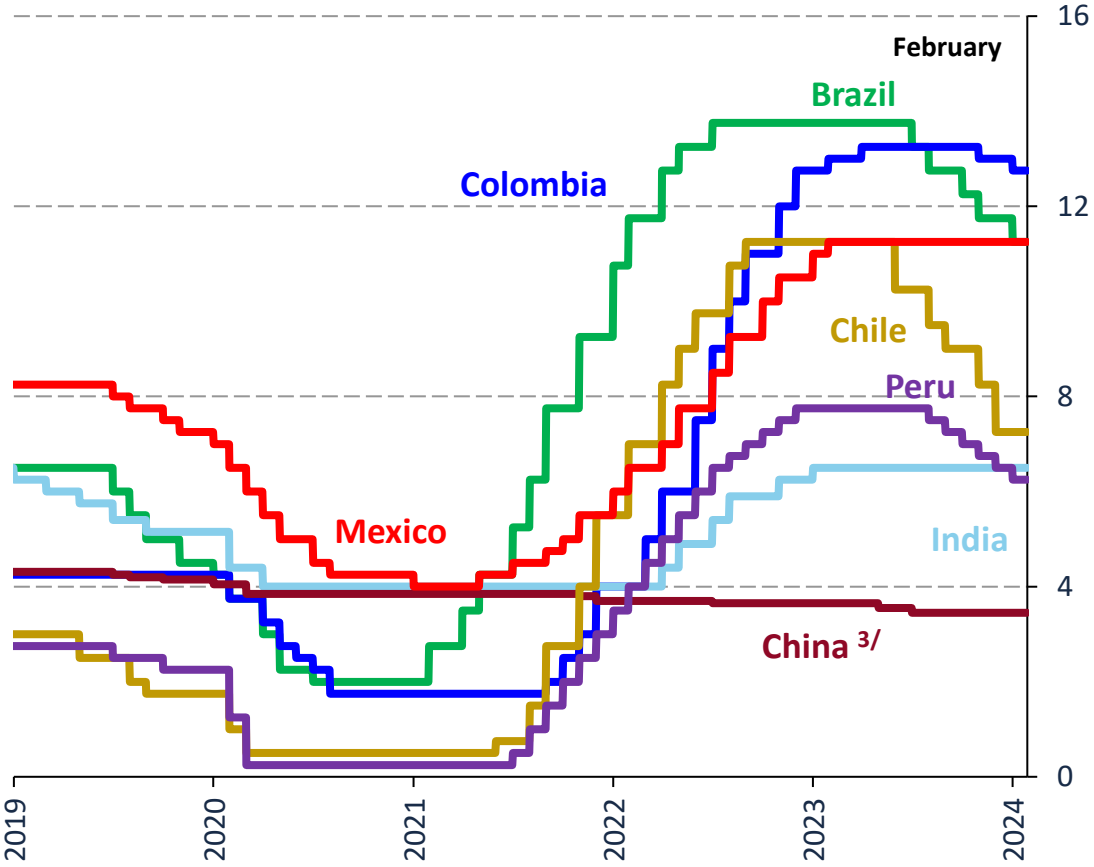
During the reference period, central banks adjusted their reference rates heterogeneously, based on the evolution of their economic indicators.

Reference rates and implied trajectories in OIS curves in advanced economies ^{1/}



^{1/} OIS: Fixed-for-floating swap where the fixed interest rate is the overnight effective reference rate. ^{2/} Data for the observed federal funds rate corresponds to the average between the lower and upper bounds of the target range.
Source: Prepared by Banco de México with data from Bloomberg.

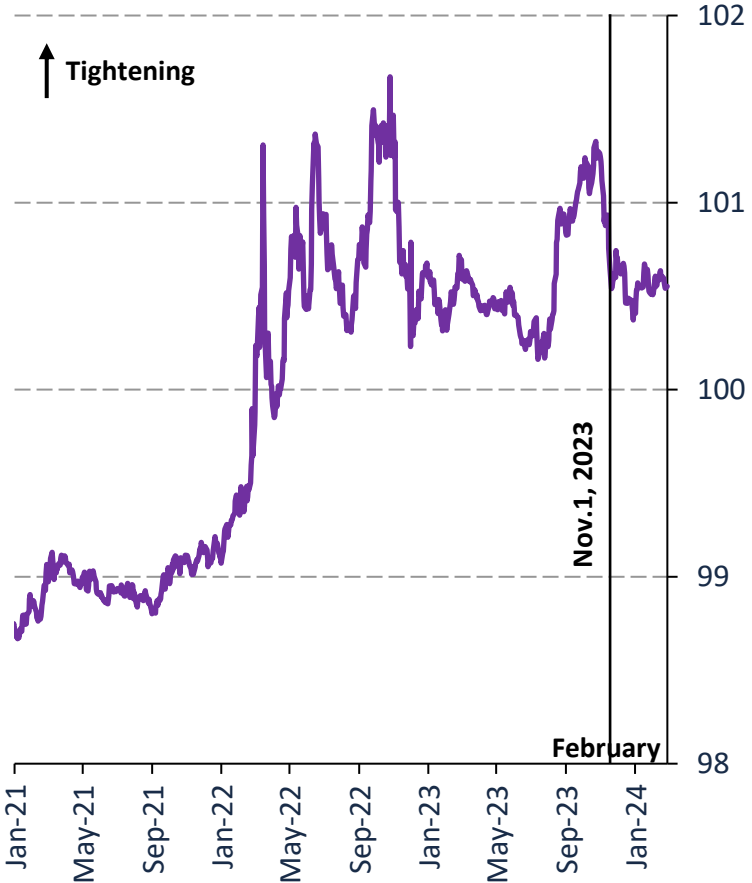
Reference rates in emerging economies %



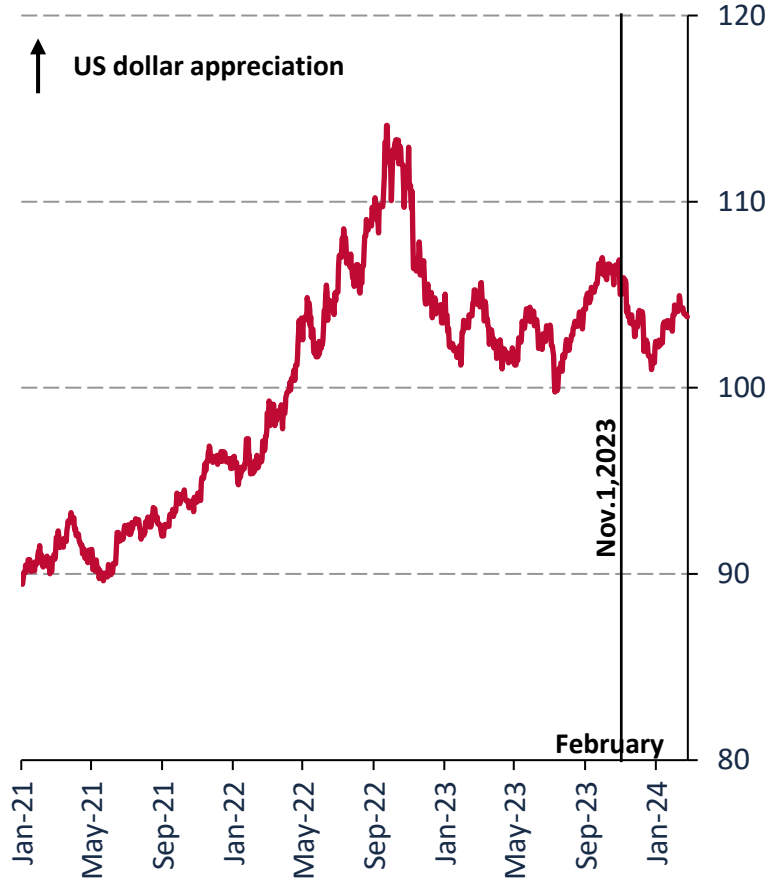
^{3/} For China, the 1-year Loan Prime Rate (LPR) is used.
Source: Haver Analytics.

During the reference period, international financial markets reacted to the expectation of a less restrictive monetary policy stance than that anticipated in the United States at the end of Q3-2023. Thus, there was some easing of financial conditions, a depreciation of the US dollar and a fall in global interest rates.

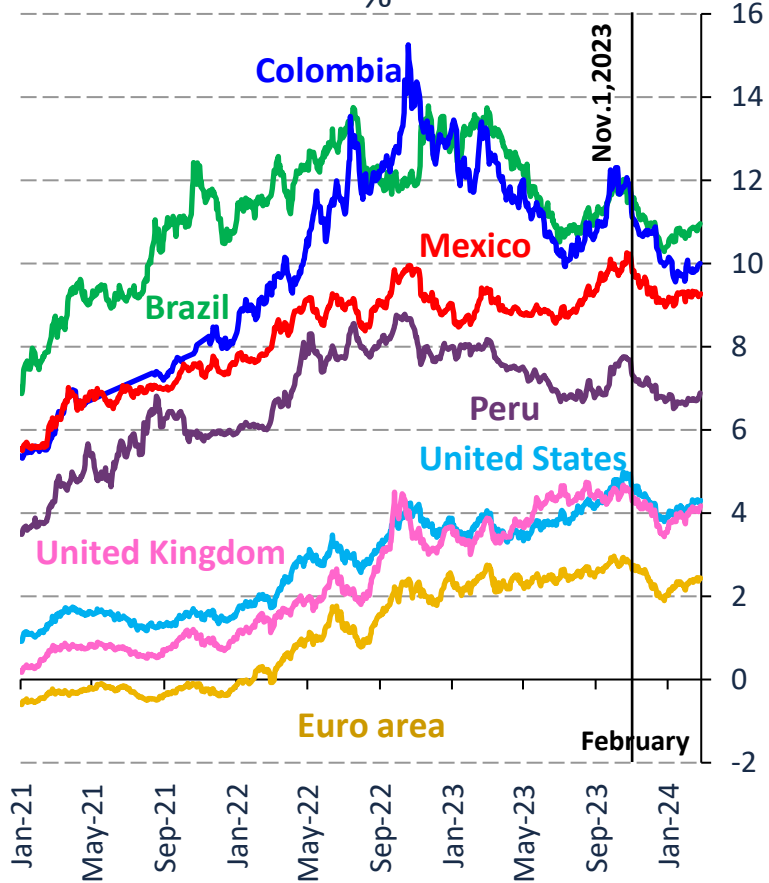
Global financial conditions index
Index



US dollar index DXY ^{1/}
Index



10-year government bond nominal interest rates
%



Source: Goldman Sachs.

^{1/} DXY: Refers to the US dollar index calculated by the Intercontinental Exchange (ICE) as a weighted average of the nominal exchange rate of six currencies: euro, Japanese yen, British pound, Canadian dollar, Swedish krona, and Swiss franc.
Source: Bloomberg.

Source: Prepared by Banco de México with data from Bloomberg and Proveedor Integral de Precios (PiP).

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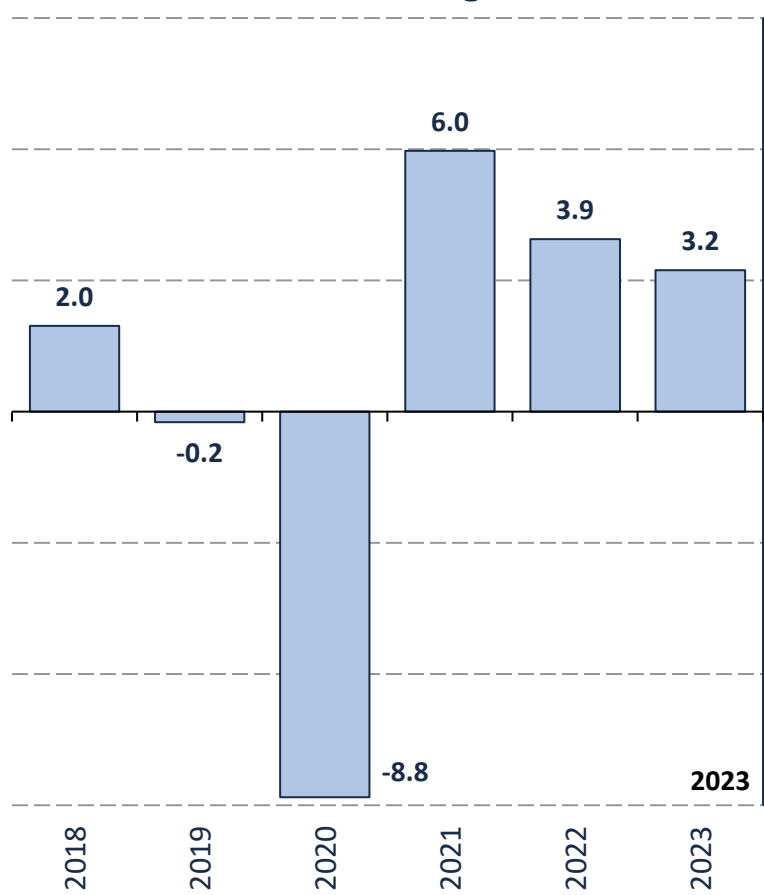
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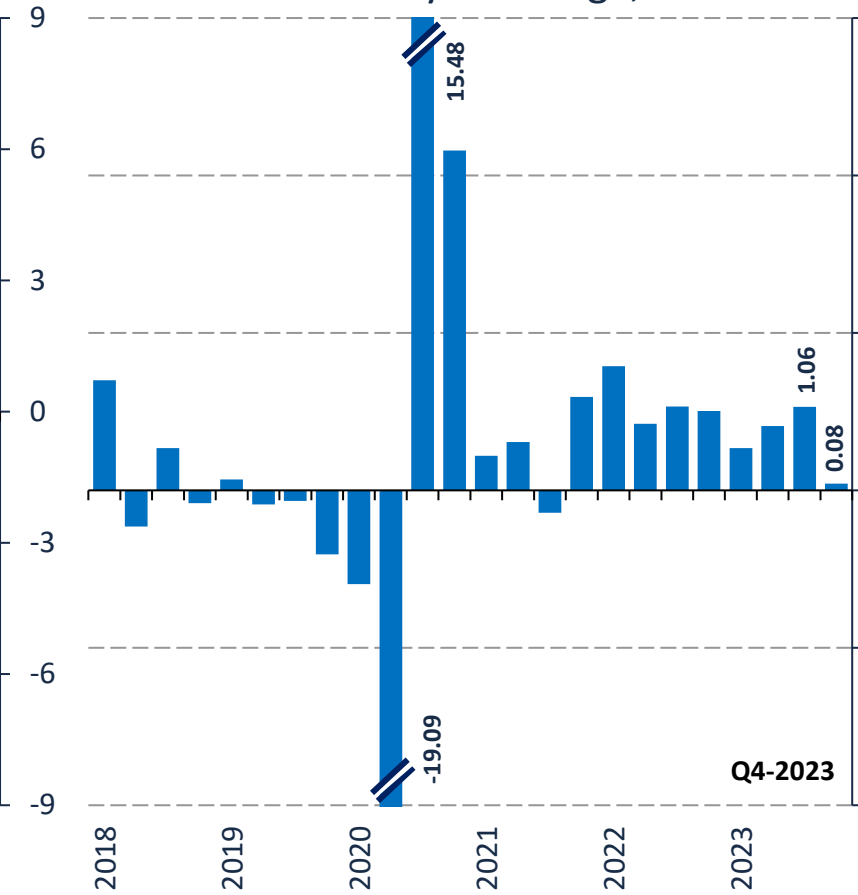
In 2023, the Mexican economy exhibited robust growth. However, it slowed markedly in Q4-2023 as a result of the weakening of the three main sectors of the economy, after having exhibited dynamism in previous quarters.

Gross Domestic Product ^{1/}

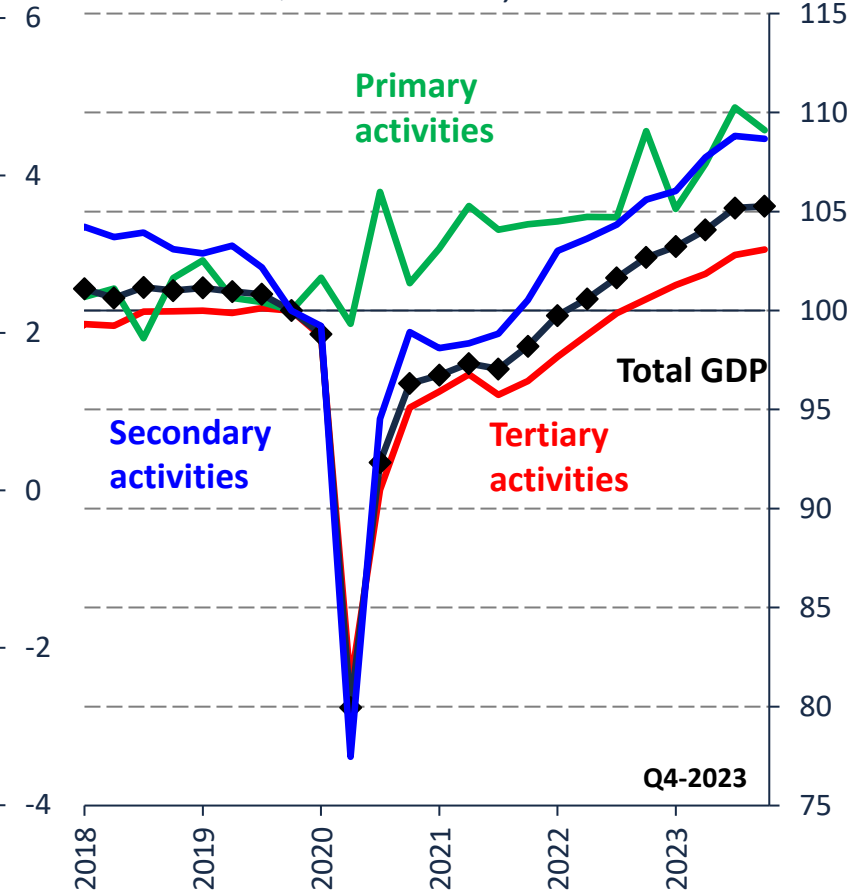
Annual % change, s. a.



Quarterly % change, s. a.



Gross Domestic Product by economic activity Q4-2019=100, s. a.



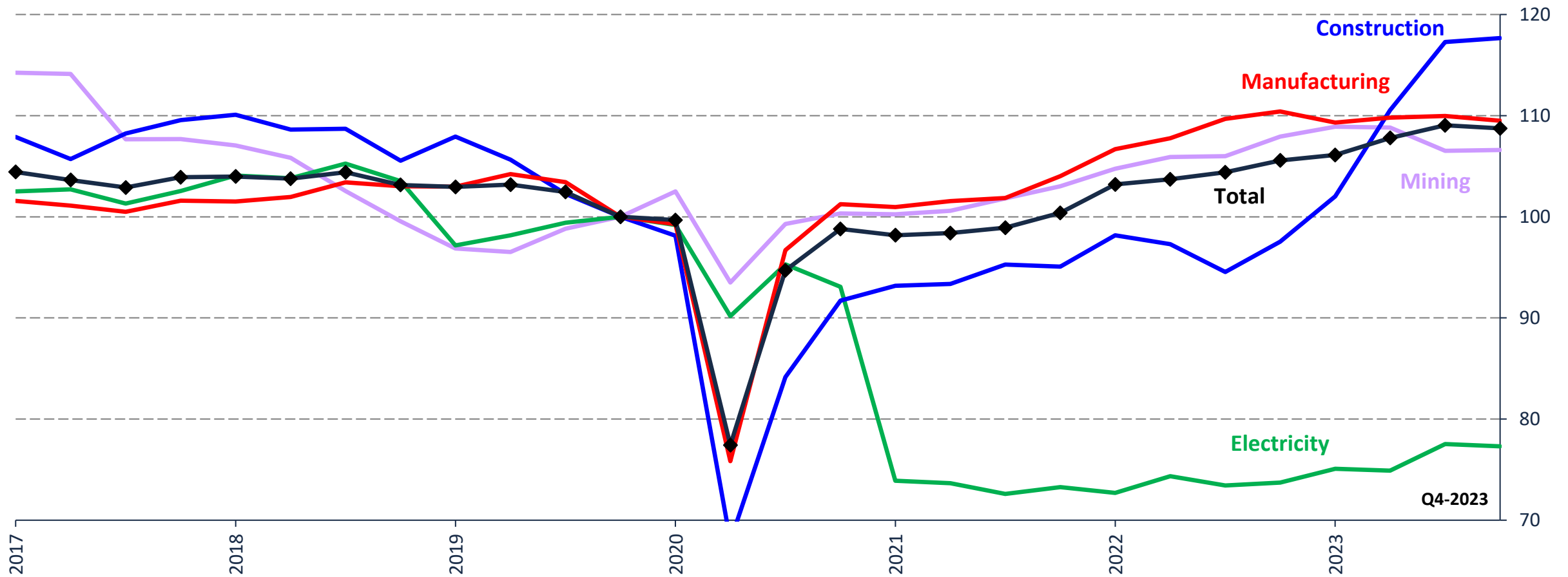
s. a. / Seasonally adjusted figures.

1/ The range of the chart has been reduced to facilitate its reading.

Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

In Q4-2023, industrial activity registered a marginal decline due to the weakness in manufacturing and the slowdown in construction.

Industrial activity
Index Q4-2019 =100, s. a.

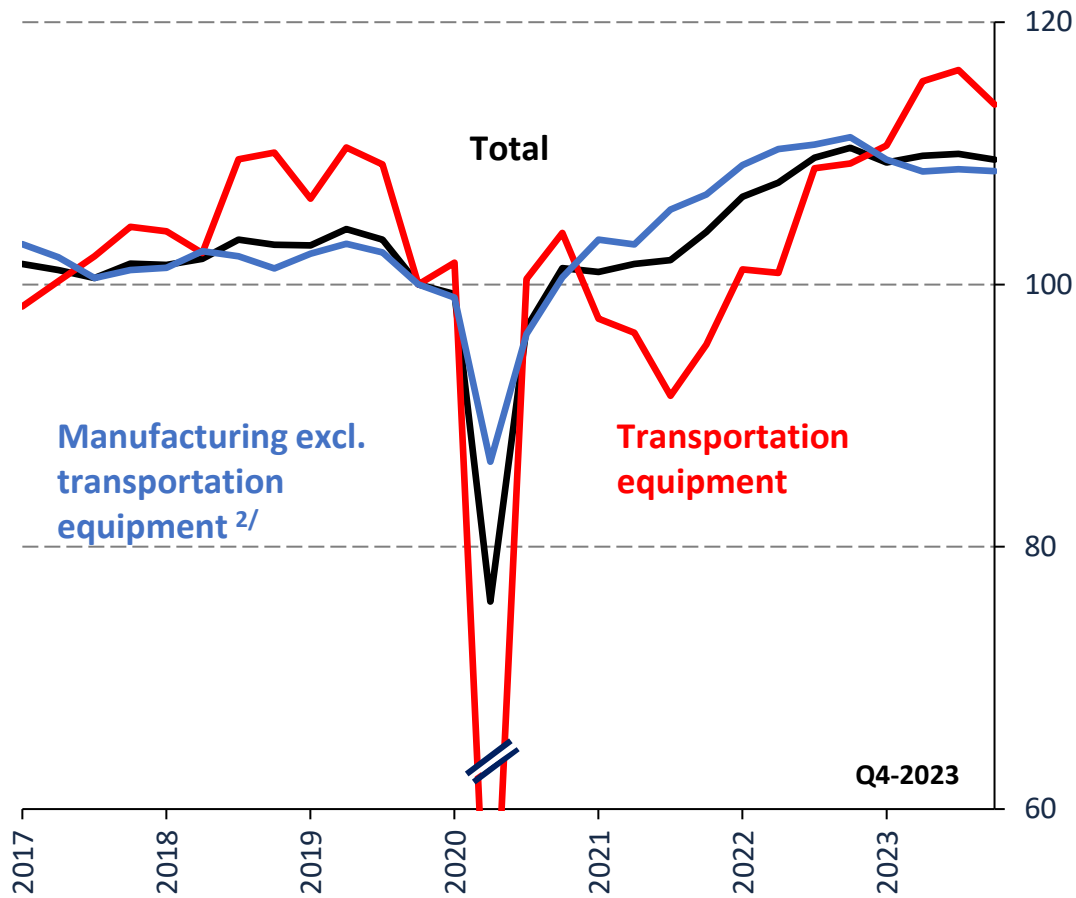


s. a. / Seasonally adjusted figures.

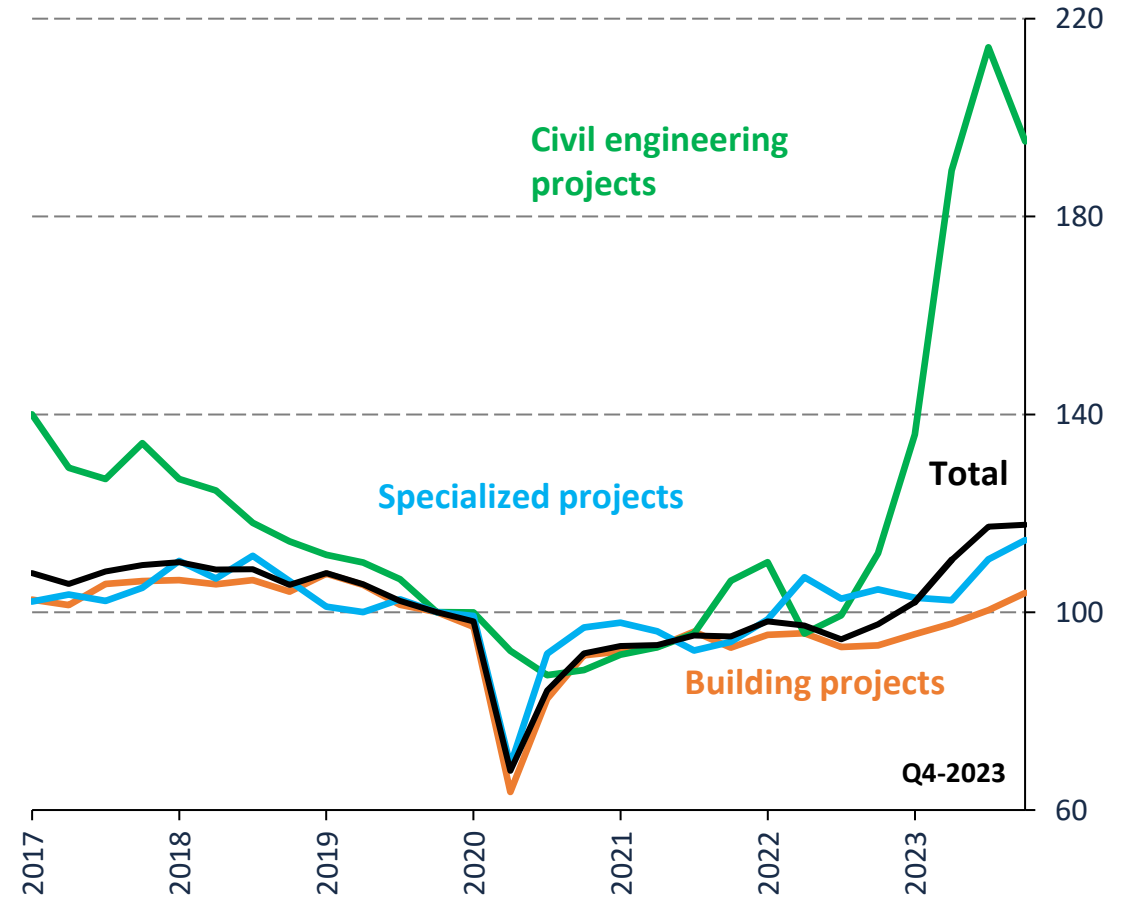
Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish) and INEGI.

Regarding manufacturing, in Q4-2023, the production of transportation equipment declined, while the remaining subsectors continued showing sluggishness. As for construction, civil engineering projects remained at historically high levels, although they declined during the quarter.

Manufacturing production ^{1/}
Index Q4-2019 =100, s.a.



Construction production
Index Q4-2019 =100, s.a.



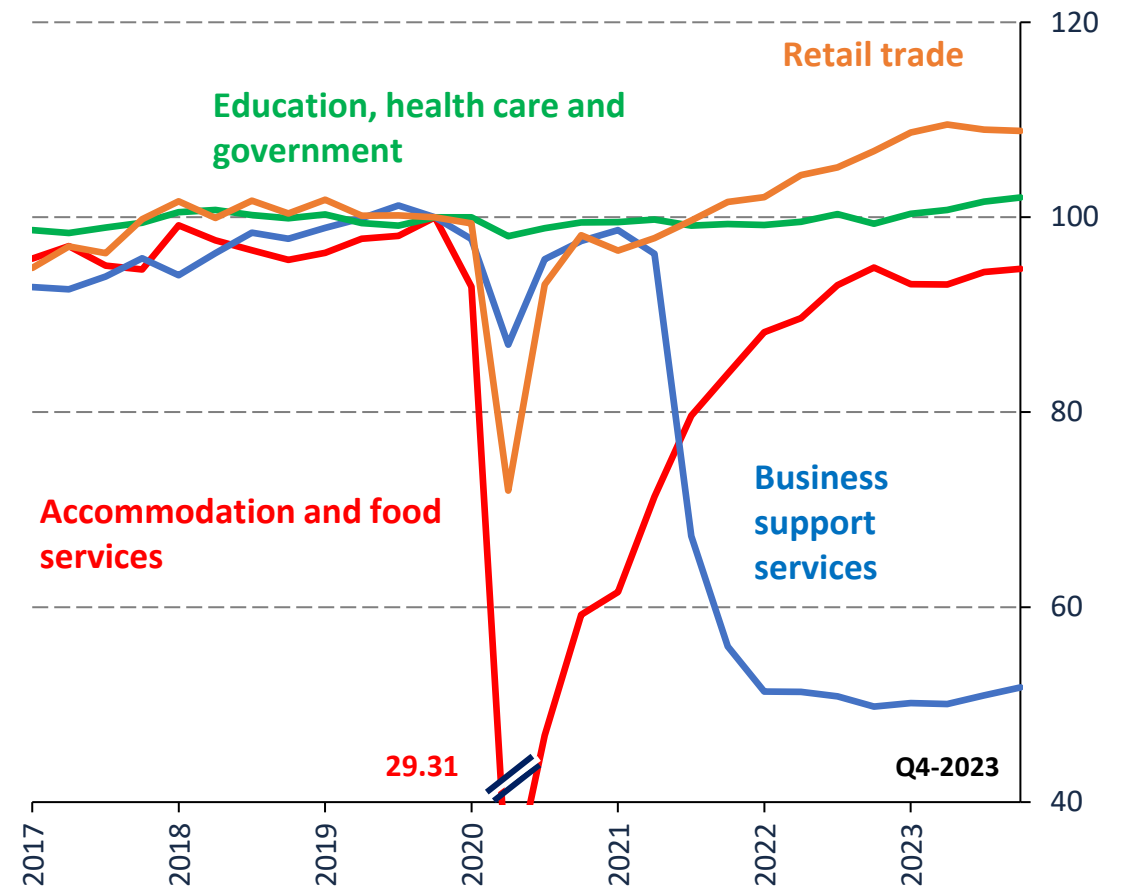
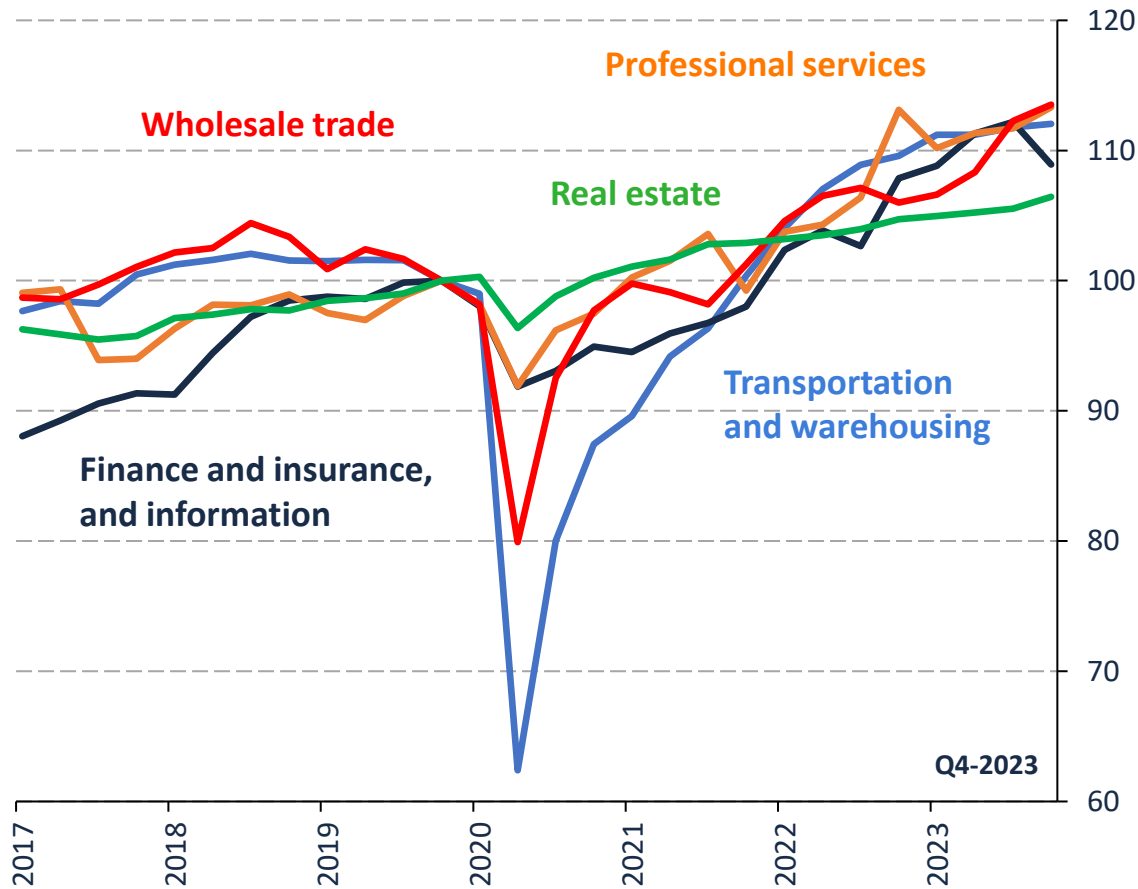
s. a. / Seasonally adjusted figures.

1/ The range of the chart has been reduced to facilitate its reading. 2/ Prepared and seasonally adjusted by Banco de México with INEGI data.

Source: Monthly Industrial Activity Indicator, Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

In Q4-2023, services grew slightly. There was a heterogeneous behavior among its components.

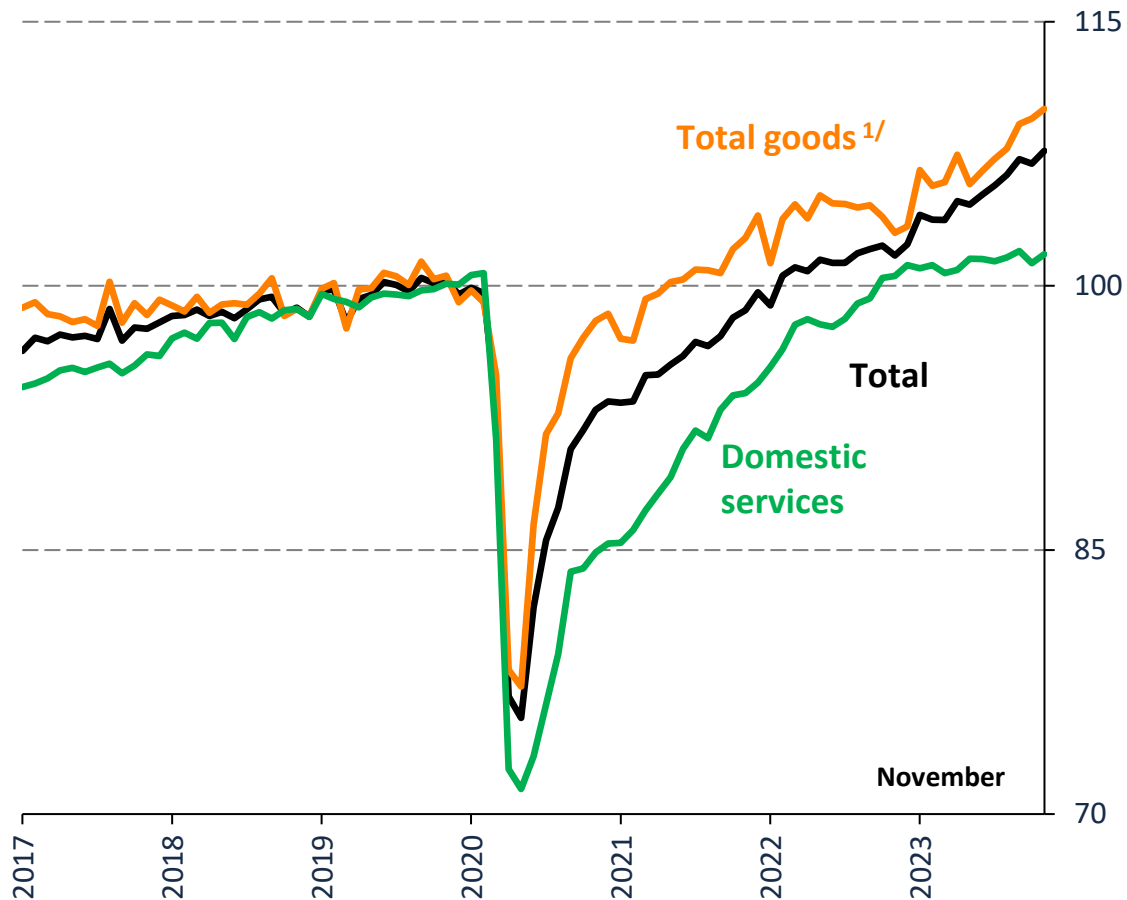
IGAE services^{1/}
Index Q4-2019=100, s. a.



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

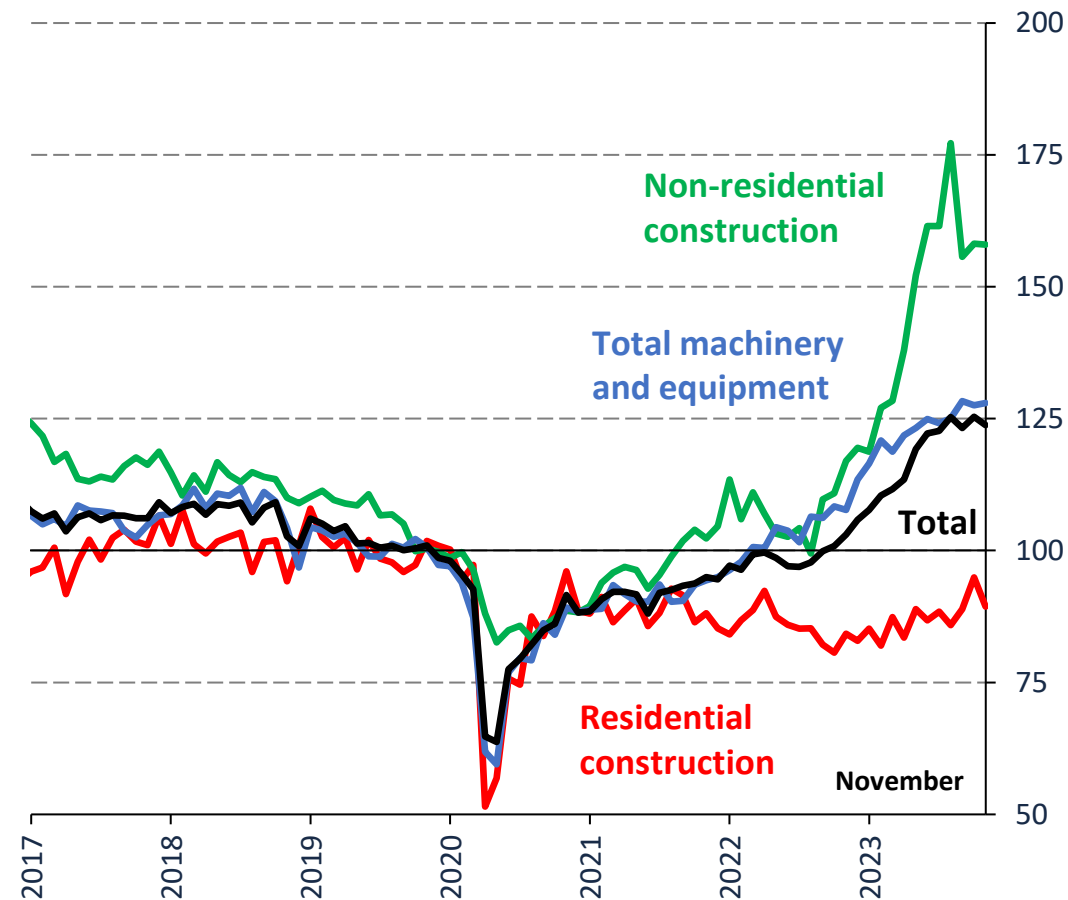
During the October-November period, private consumption continued trending upwards. Gross fixed investment decelerated, after having remained strong in previous quarters.

Total private consumption
Index Q4-2019=100, s. a.



s. a. / Seasonally adjusted figures.
1/ Includes both national and imported goods. Prepared and seasonally adjusted by Banco de México.
Source: Mexico's National Accounts System (SCNM, for its acronym in Spanish), INEGI.

Investment
Index Q4-2019=100, s. a.



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

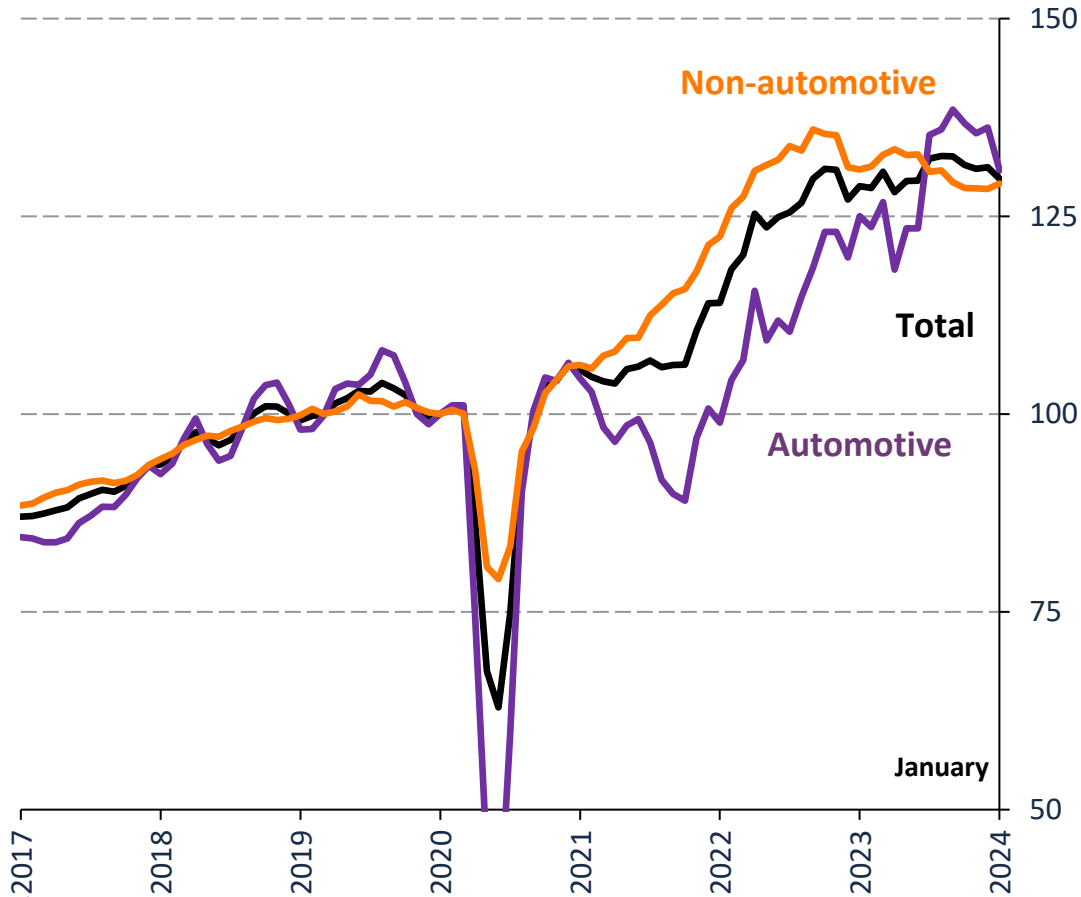
In Q4-2023 and early 2024, manufacturing exports declined with respect to the previous quarter. This was the result of decreases in both automotive and non-automotive exports.

Manufacturing exports ^{1/}

Three-month moving average

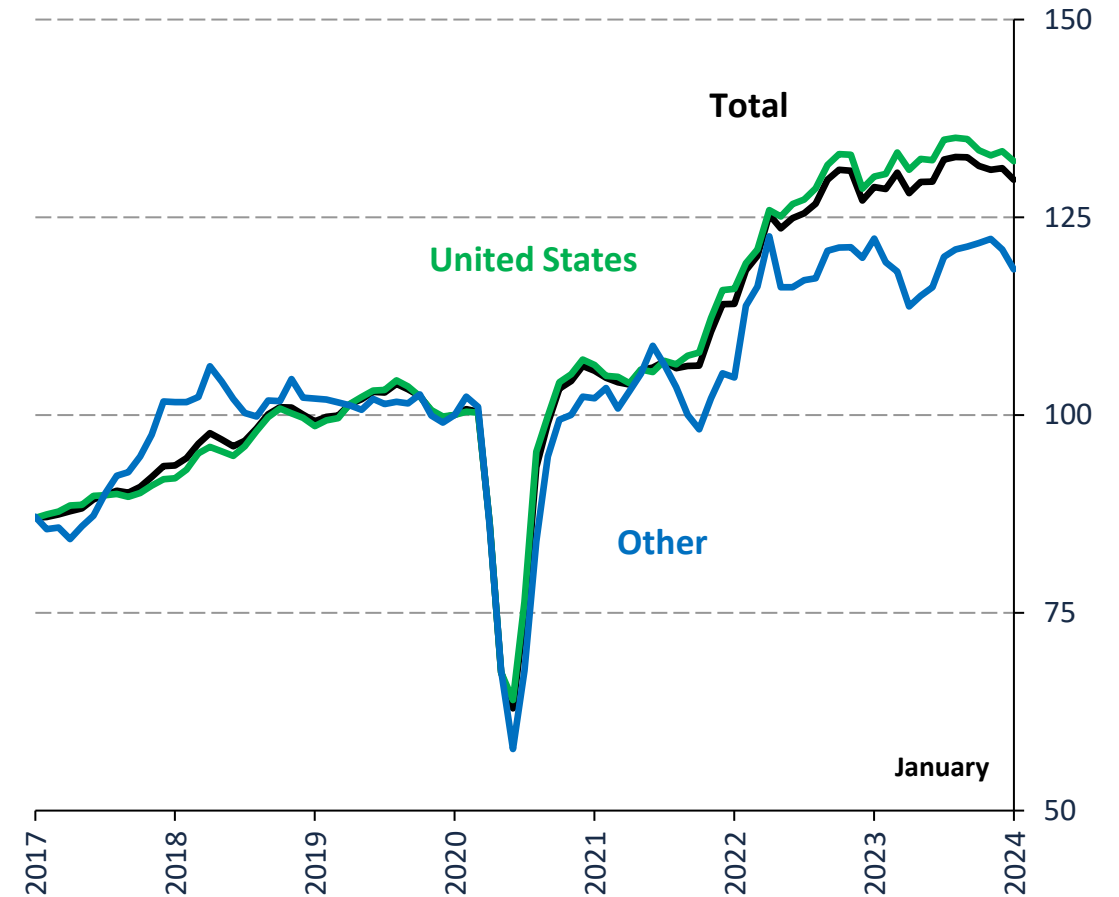
Automotive and non-automotive manufacturing exports ^{2/}

Index Jan-2020=100, s. a.



By destination

Index Jan-2020=100, s. a.

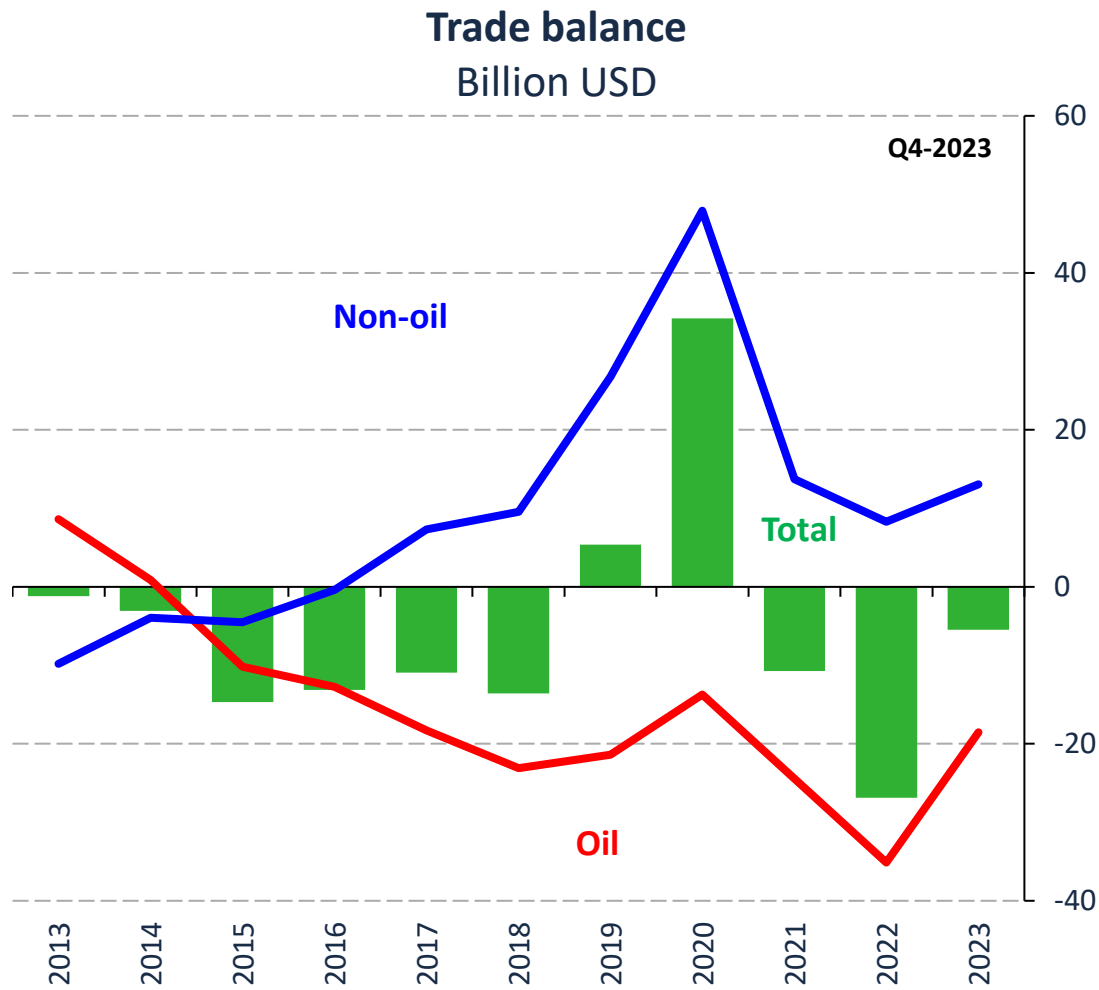


s. a. / Seasonally adjusted figures.

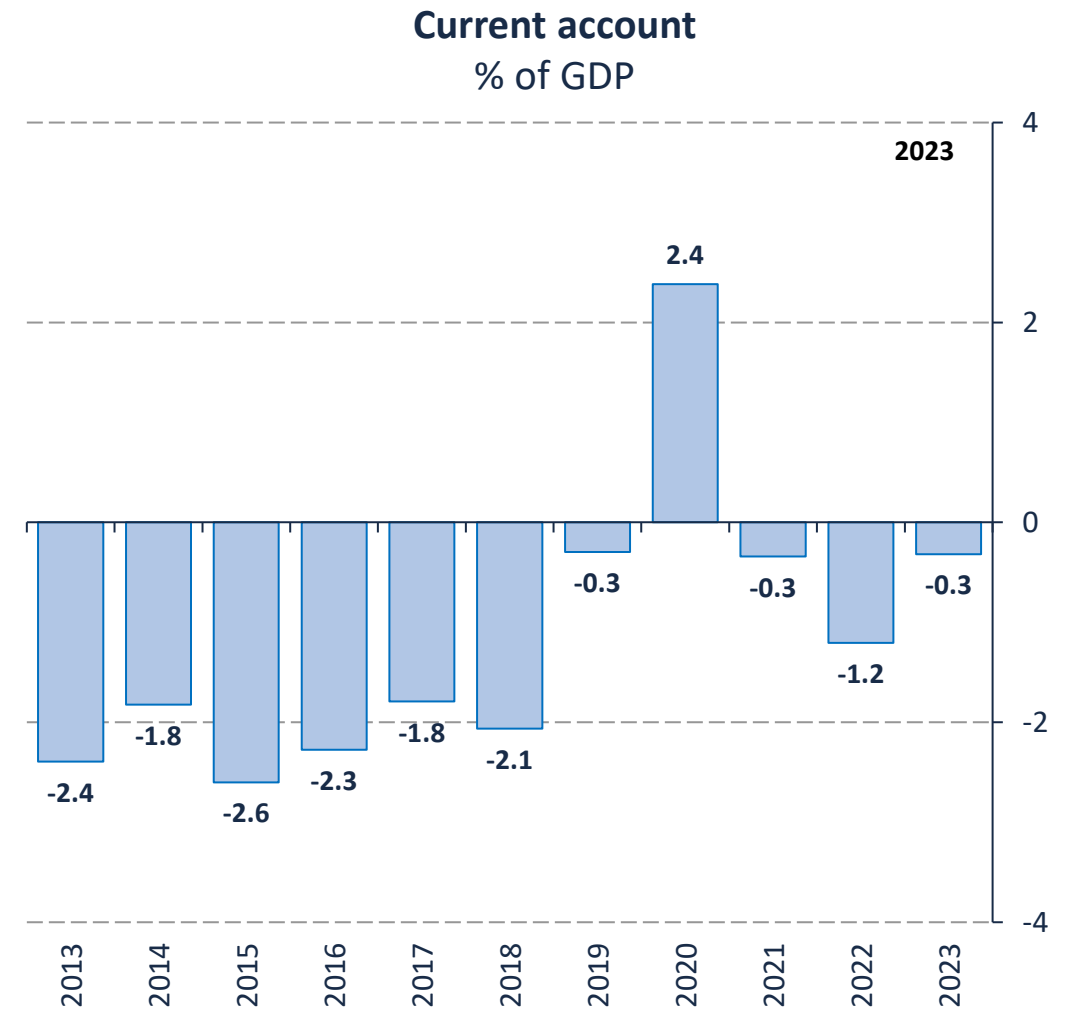
1/ Based on current US dollars. 2/ The range of the chart has been reduced to facilitate its reading.

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.

In 2023, the current account registered a smaller deficit than in 2022, thus remaining at moderate levels.



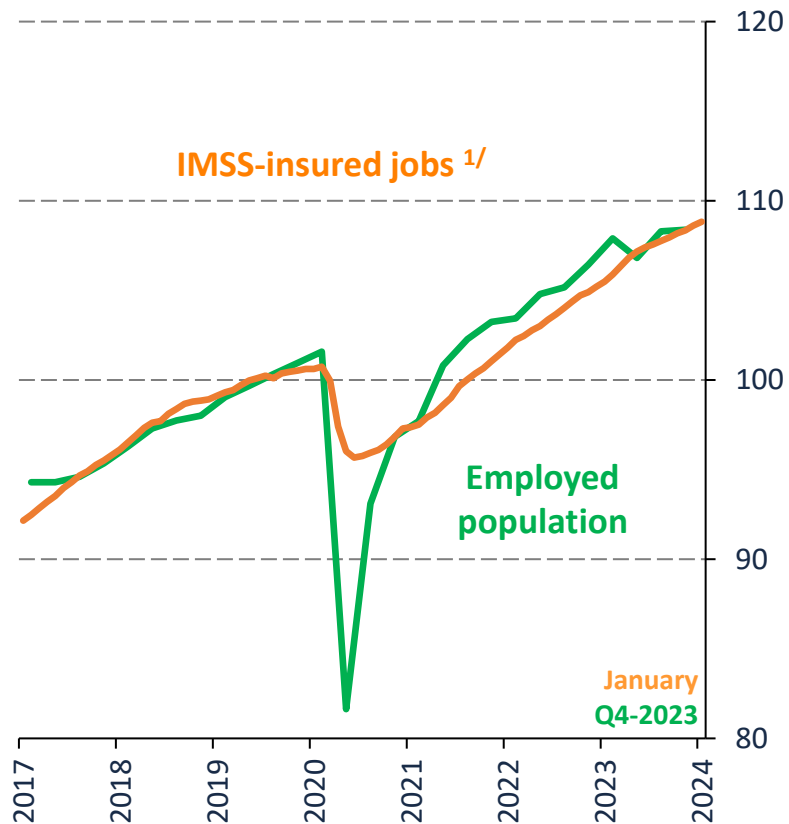
Source: SAT, SE, Banco de México, INEGI. Mexico's Merchandise Trade Balance. SNIEG. Information of national interest.



Source: Banco de México and INEGI.

The labor market continued exhibiting strength during Q4-2023.

IMSS-insured jobs and employed population
Index 2019=100, s. a.



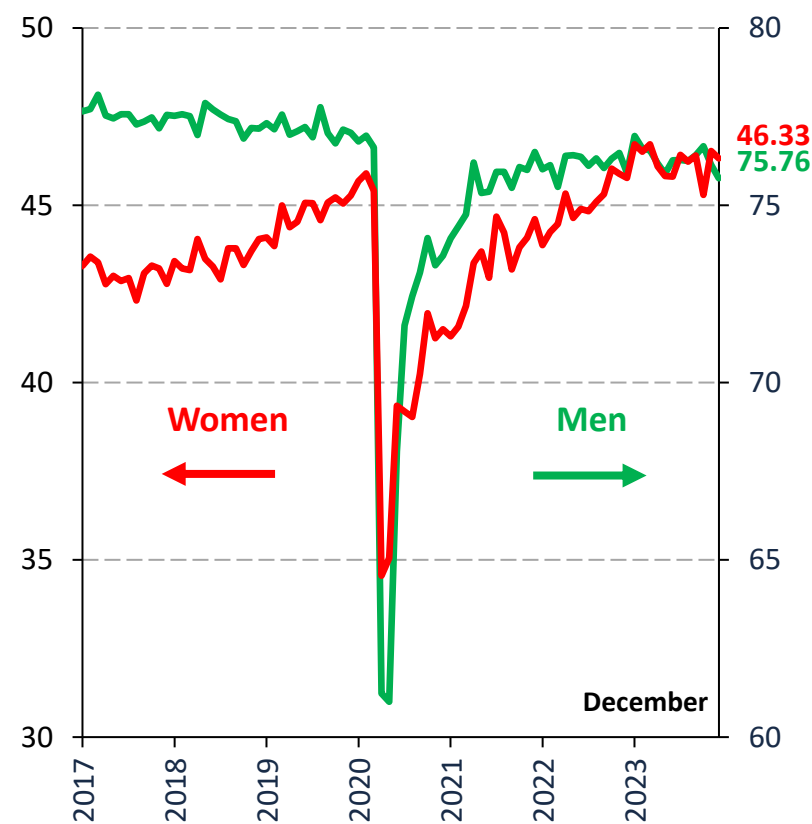
s. a. / Seasonally adjusted figures.
1/ Refers to permanent and temporary urban workers. Seasonal adjustment by Banco de México.
Source: Prepared by Banco de México with data from IMSS and INEGI (ENOE).

National unemployment rate
%, s. a.



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

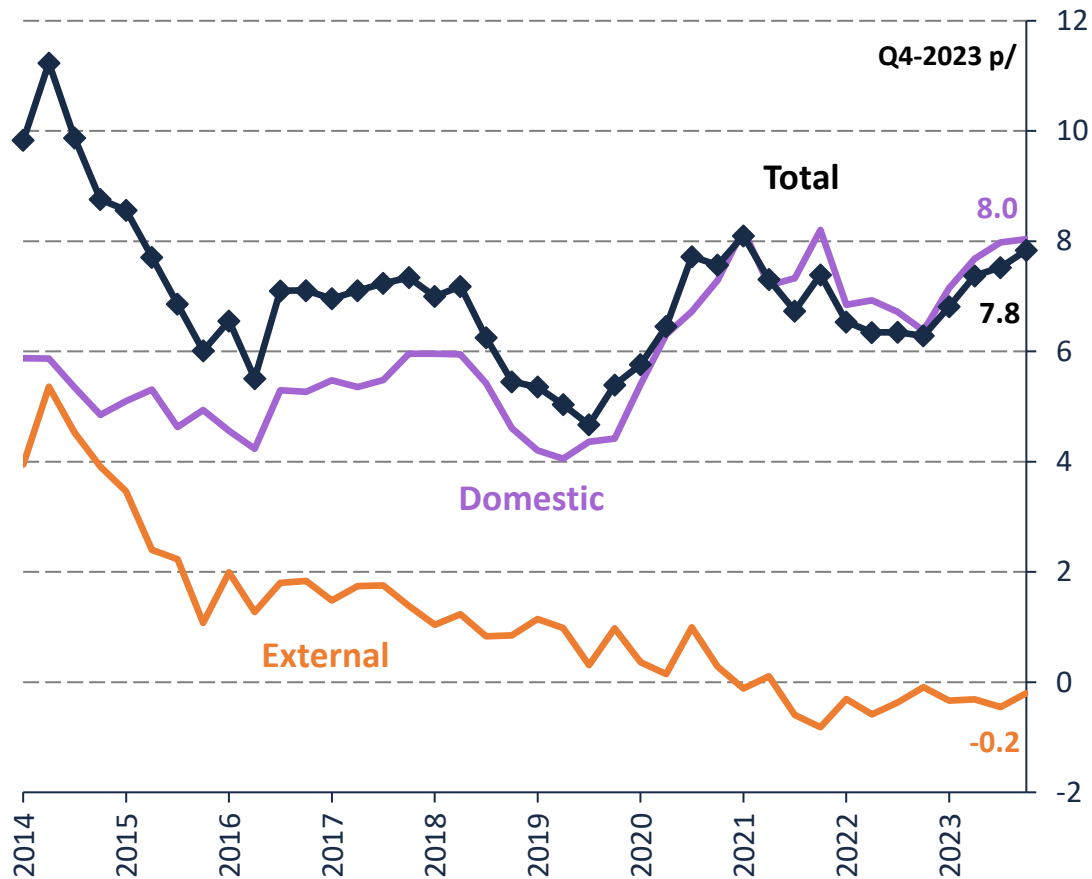
National labor participation rates ^{2/}
Three-month moving average, %, s. a.



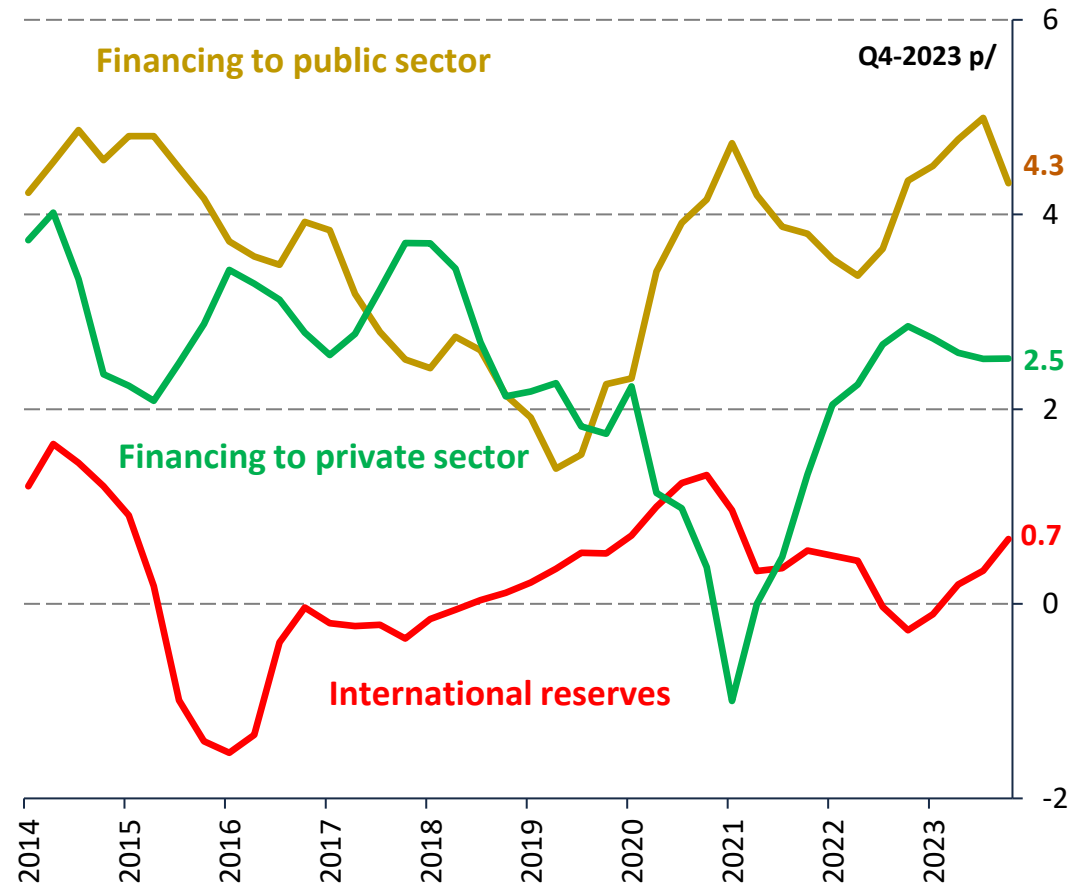
s. a. / Seasonally adjusted figures.
2/ Percentage of the economically active population (EAP) with respect to the population 15 years and older.
Source: Prepared by Banco de México with data from INEGI (ENOE).

Domestic financing flows to both the public and private sectors continued at high levels in Q4-2023, although they slightly moderated with respect to the previous quarter.

Sources of funds in the economy
Annual flows as a percentage of GDP



Uses of funds in the economy
Annual flows as a percentage of GDP



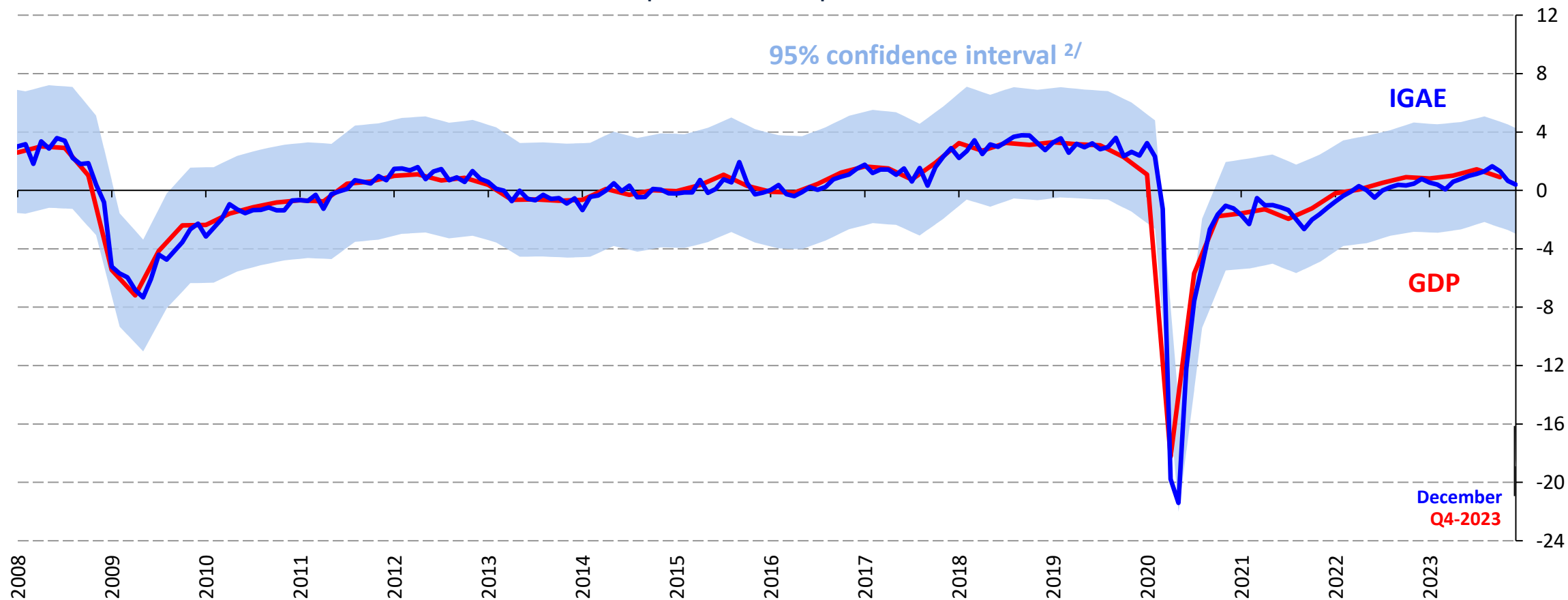
p/ Preliminary figures.

Note: See Table 5 of this Quarterly Report (Sources and Uses of Funds in the Economy) for a description of the concepts.

Source: Banco de México.

While the point estimate of the output gap remained positive, it decreased marginally in Q4-2023.

Output gap point estimate ^{1/} % of potential output, s. a.



s. a. / Prepared with seasonally adjusted data.

1/Output gap estimated with a tail-corrected Hodrick-Prescott filter; see "Inflation Report April – June 2009", Banco de México, p.69.

2/Output gap confidence interval calculated with a method of unobserved components.

Source: Prepared by Banco de México with data from INEGI and Banco de México.

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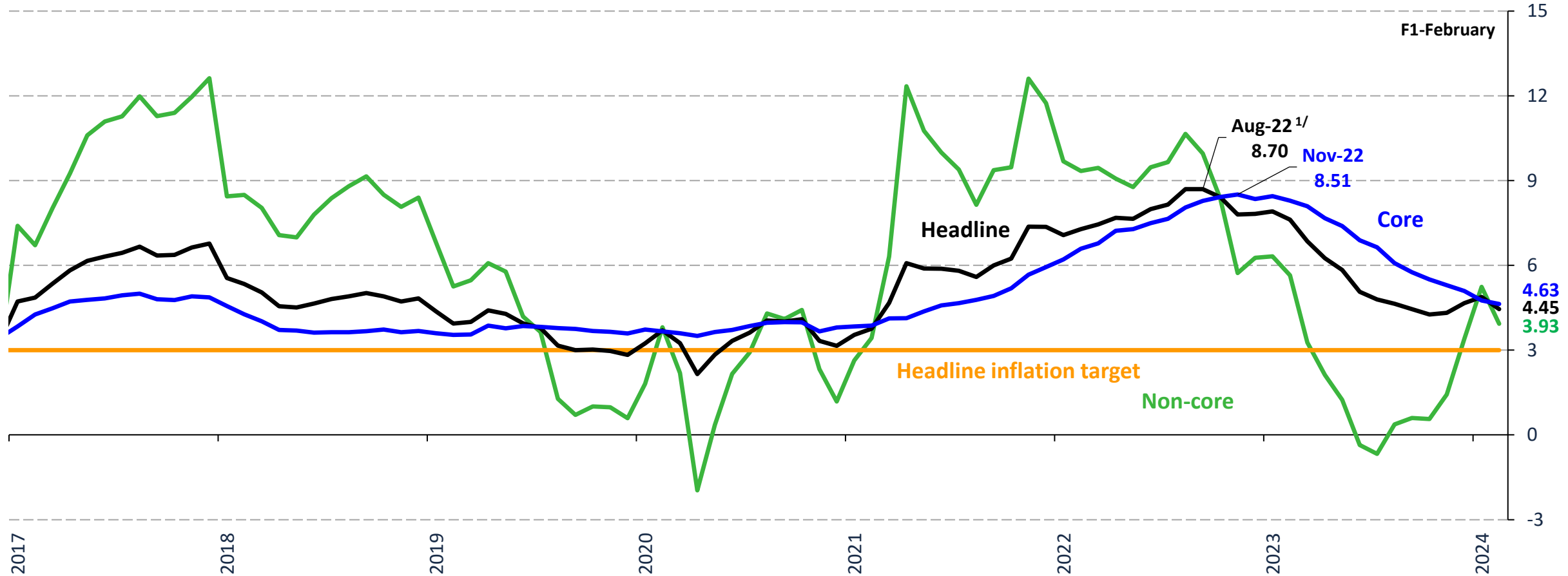
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During the period covered by this Report, both headline and core inflation were significantly below the peaks registered in the current inflationary episode.

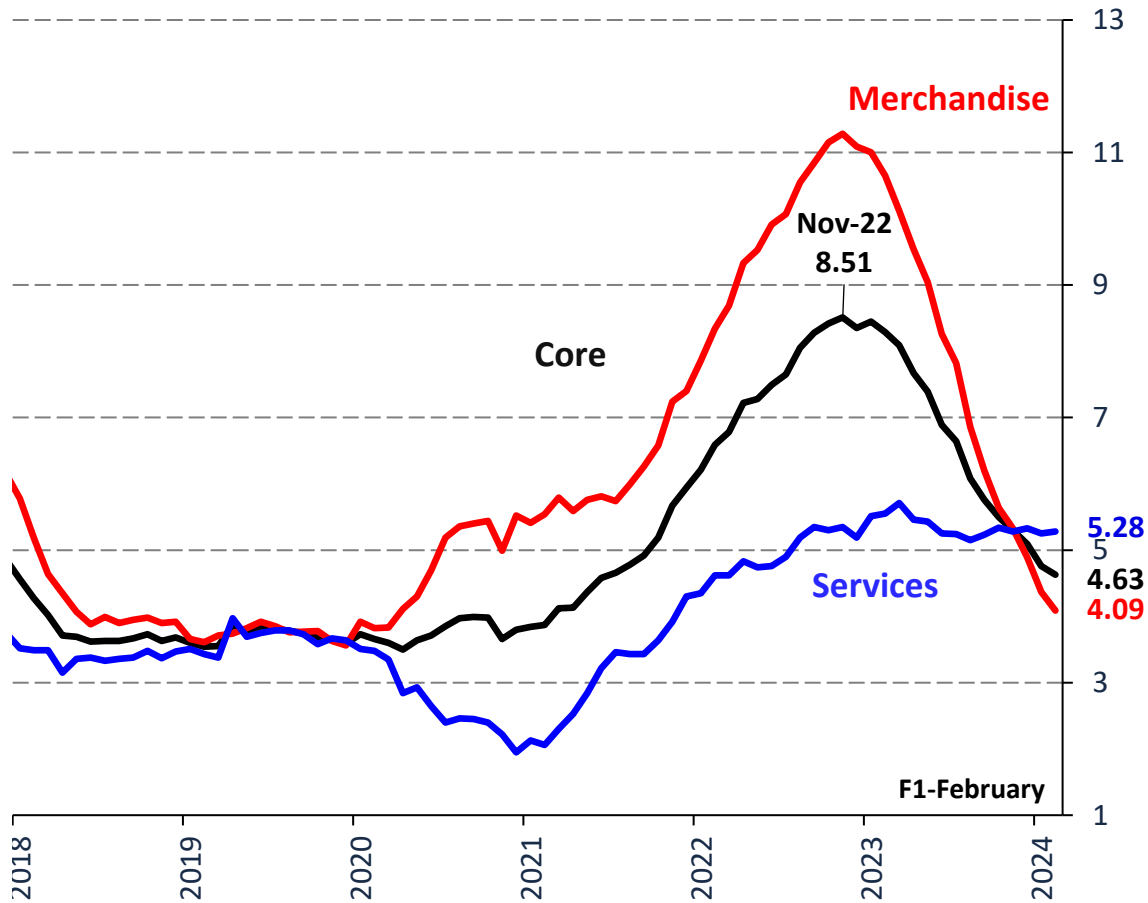
National Consumer Price Index Annual % change



1/ Headline inflation was 8.70% in August and September 2022.
Source: Banco de México and INEGI.

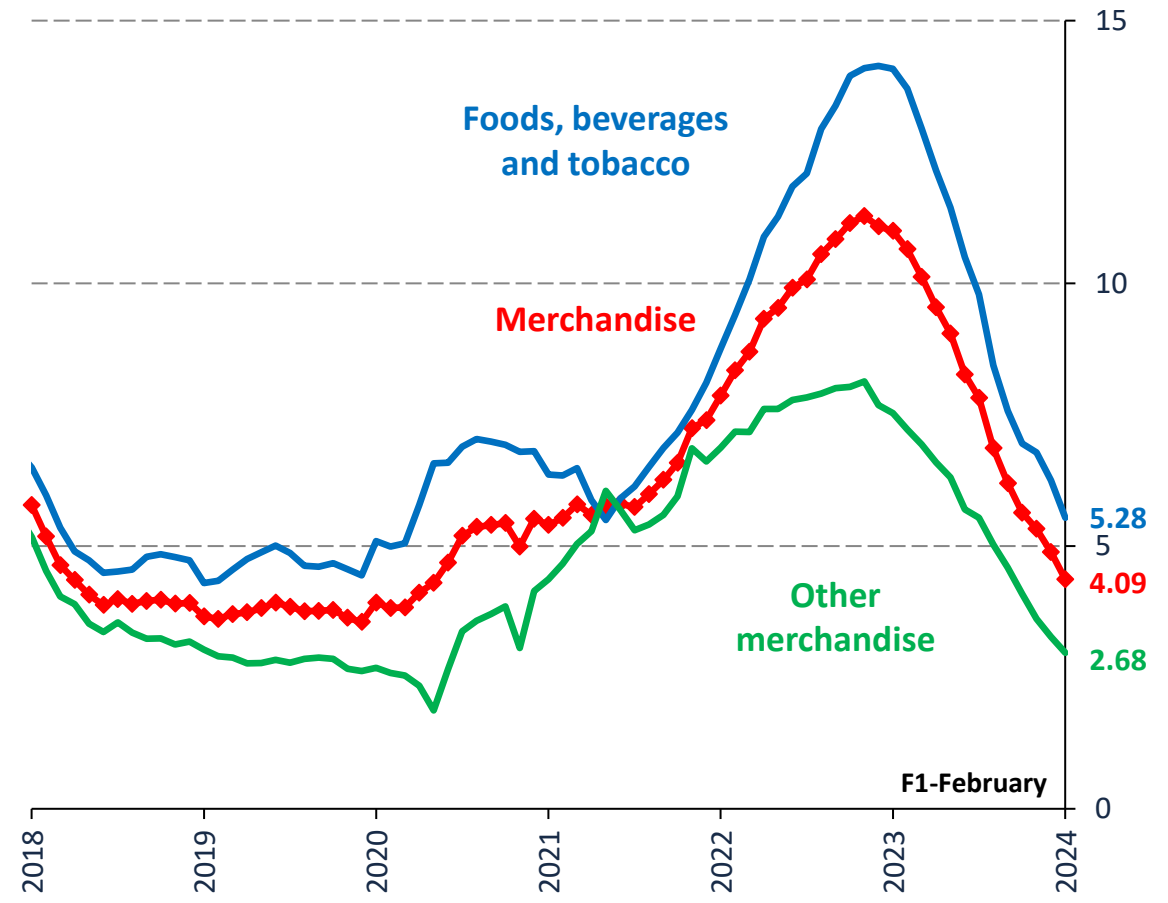
Regarding core inflation components, merchandise inflation kept a descending path, while services inflation remained at high levels and still does not show a clear downward trend.

Core price sub-index
Annual % change



Source: INEGI.

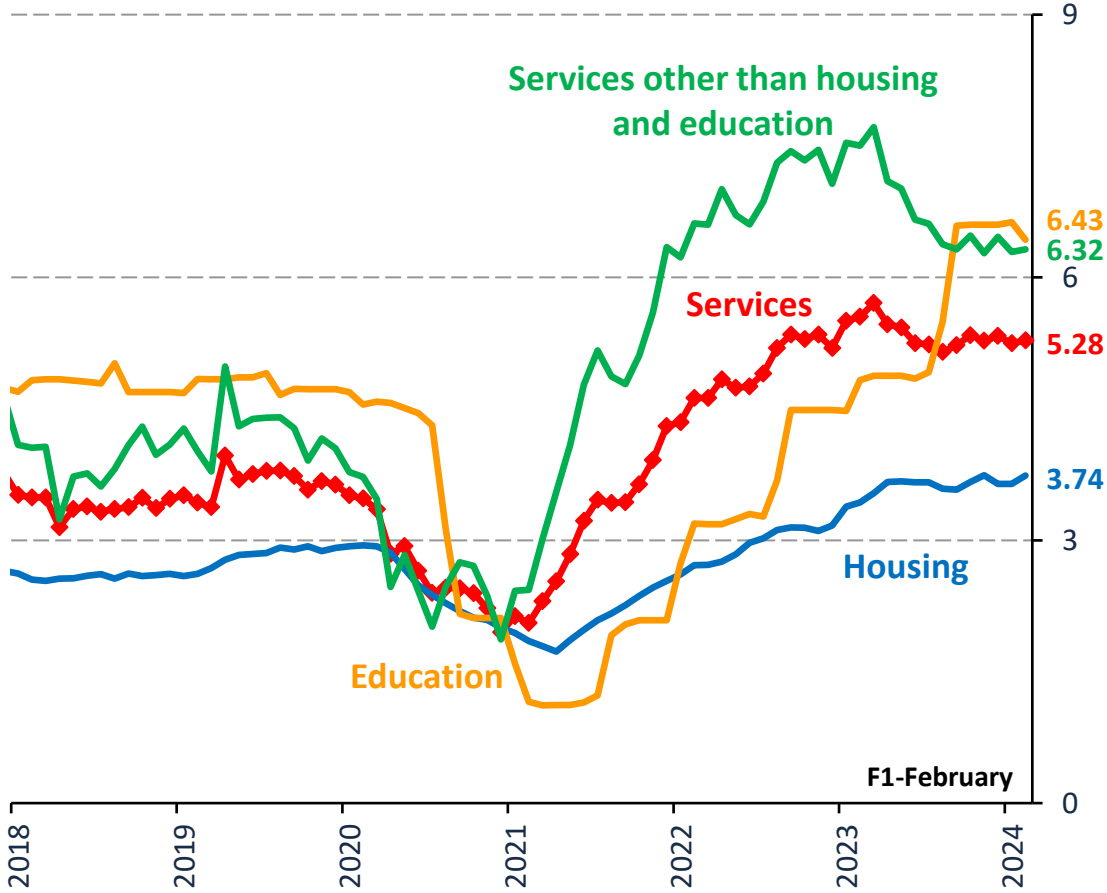
Merchandise price sub-index
Annual % change



Source: INEGI.

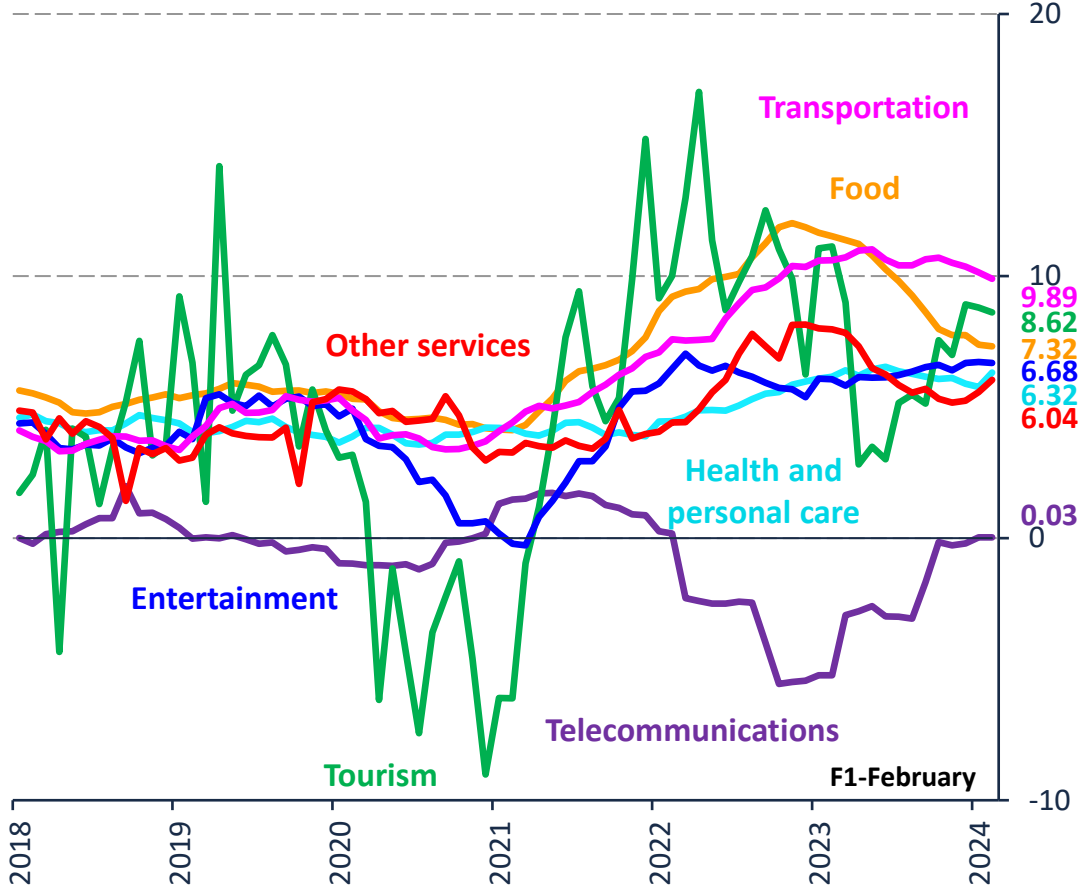
Cumulative cost-related pressures continued affecting inflation of different services in a delayed manner, as demand for these has been recovering after the lockdown.

Services price sub-index
Annual % change



Source: INEGI.

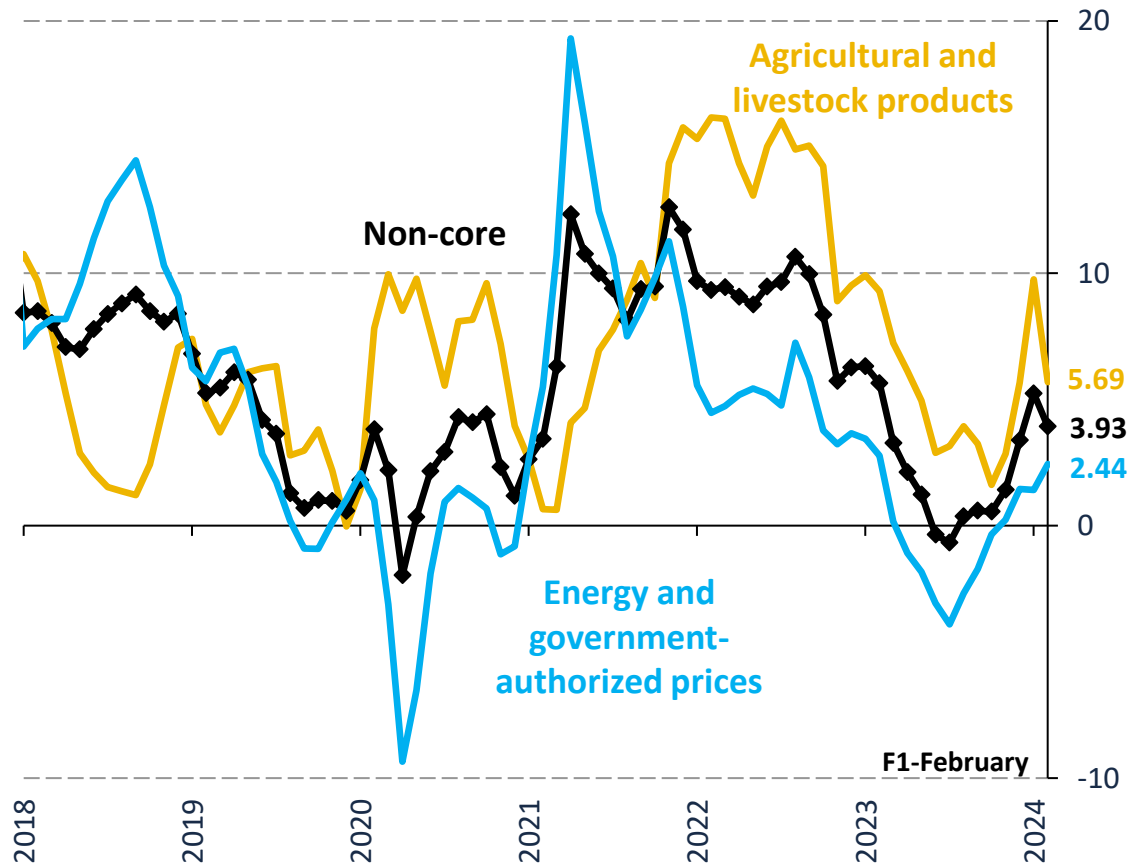
Services excluding housing and education
Annual % change



Source: INEGI.

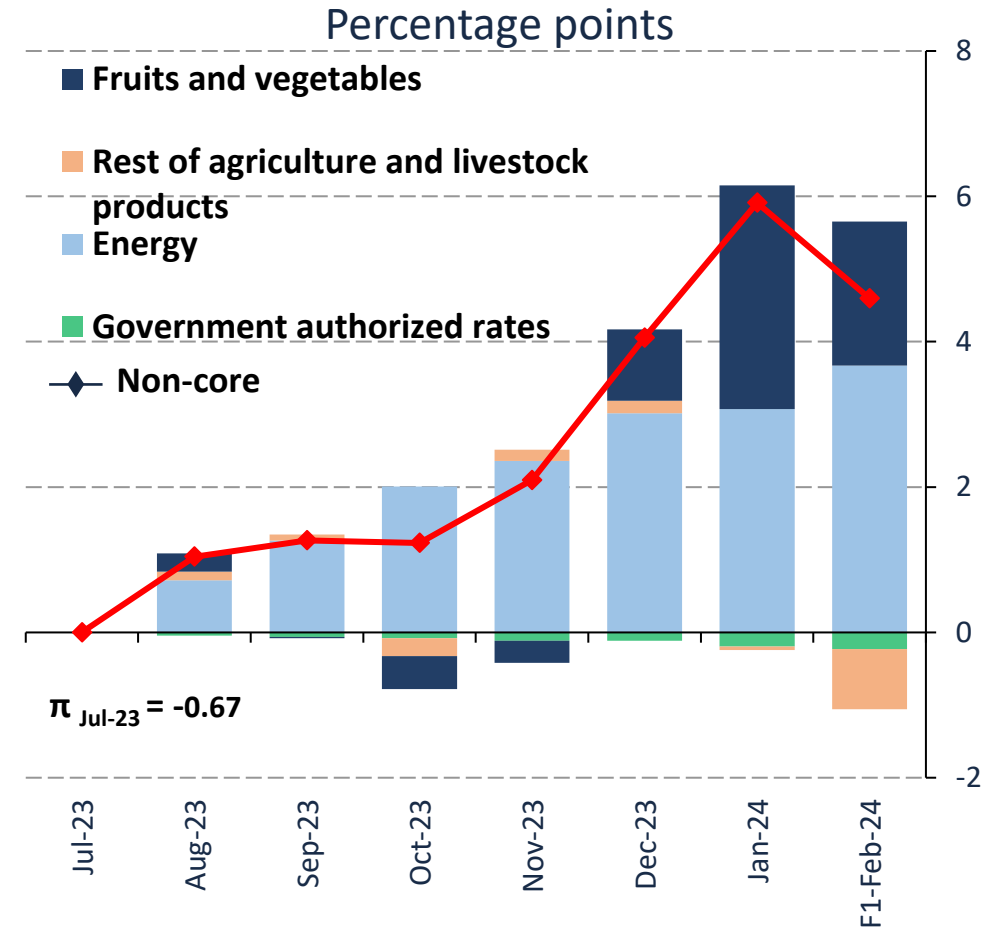
In late 2023 and January 2024, annual non-core inflation increased, driven by the higher prices of energy products and of fruit and vegetables. Nevertheless, in the first fortnight of February 2024, non-core inflation slightly reversed.

Non-core price sub-index
Annual % change



Source: INEGI.

Change in annual inflation incidence with respect to July 2023



Note: Annual variation in July 2023 was -0.67%, the lowest since April 2020 when it located at -1.96%. The sum of incidences might differ from total due to rounding of figures. Source: INEGI.

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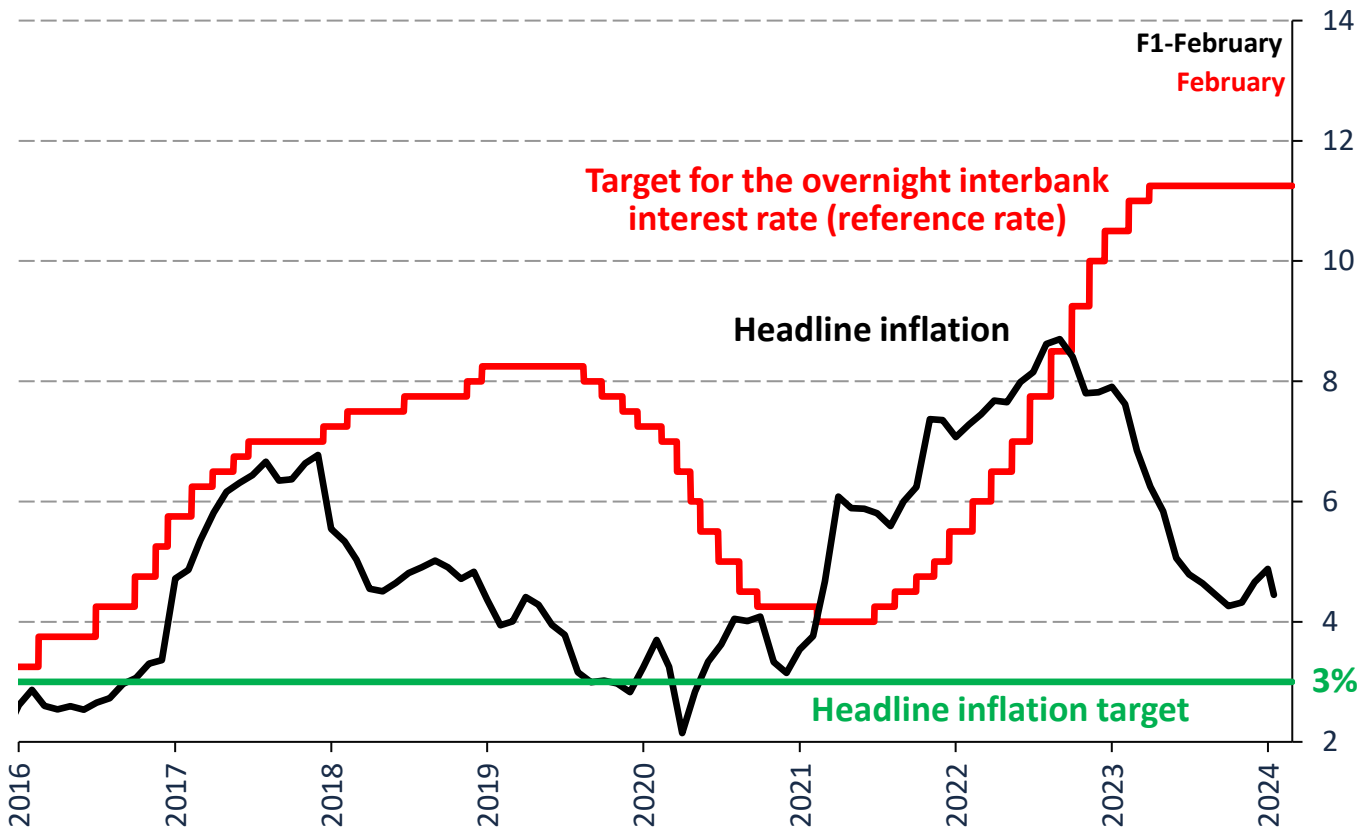
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In the monetary policy meetings of the reported period, the Governing Board decided unanimously to keep the reference rate unchanged at 11.25%.

Recent evolution of Banco de México's monetary policy decisions

Target for the overnight interbank interest rate and headline inflation
Annual %



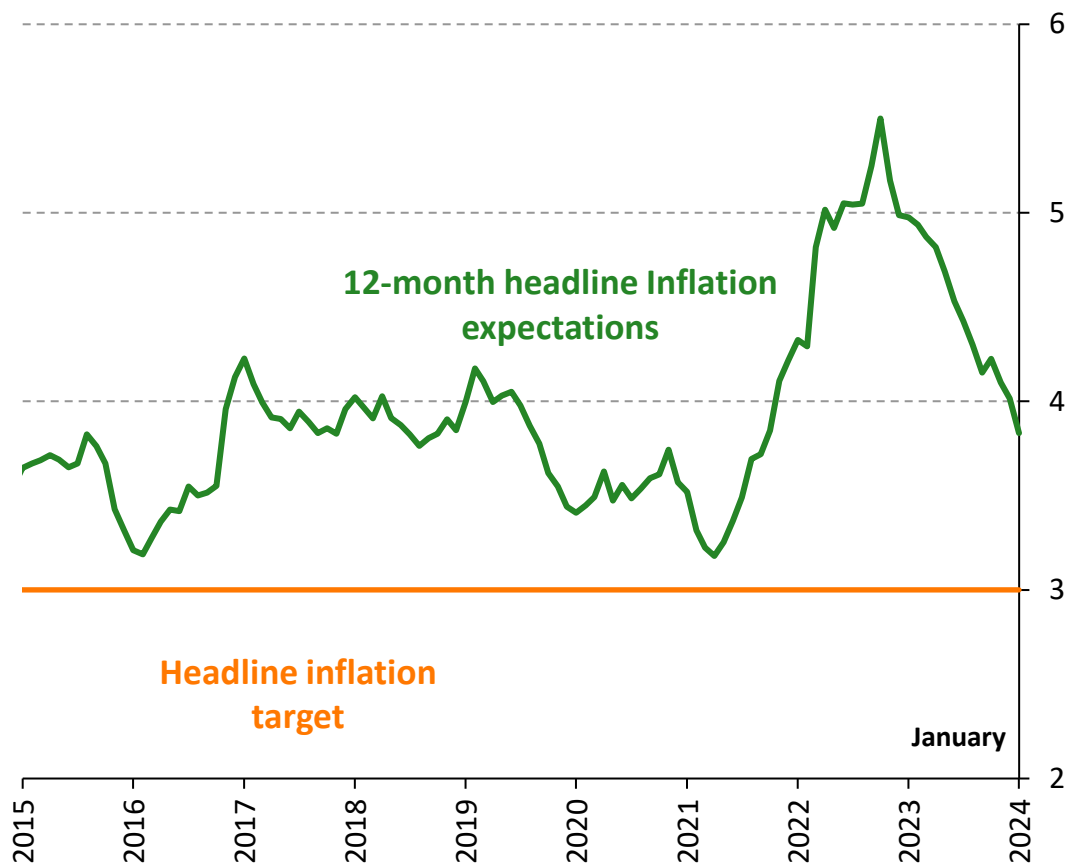
Source: Banco de México and INEGI.

	Changes in the reference rate (pb)	Interest rate (%)
Mar-21	0	4.00
May-21	0	4.00
Jun-21	+25	4.25
Aug-21	+25	4.50
Sep-21	+25	4.75
Nov-21	+25	5.00
Dec-21	+50	5.50
Feb-22	+50	6.00
Mar-22	+50	6.50
May-22	+50	7.00
Jun-22	+75	7.75
Aug-22	+75	8.50
Sep-22	+75	9.25
Nov-22	+75	10.00
Dec-22	+50	10.50
Feb-23	+50	11.00
Mar-23	+25	11.25
May-23	0	11.25
Jun-23	0	11.25
Aug-23	0	11.25
Sep-23	0	11.25
Nov-23	0	11.25
Dec-23	0	11.25
Feb-24	0	11.25

Source: Banco de México.

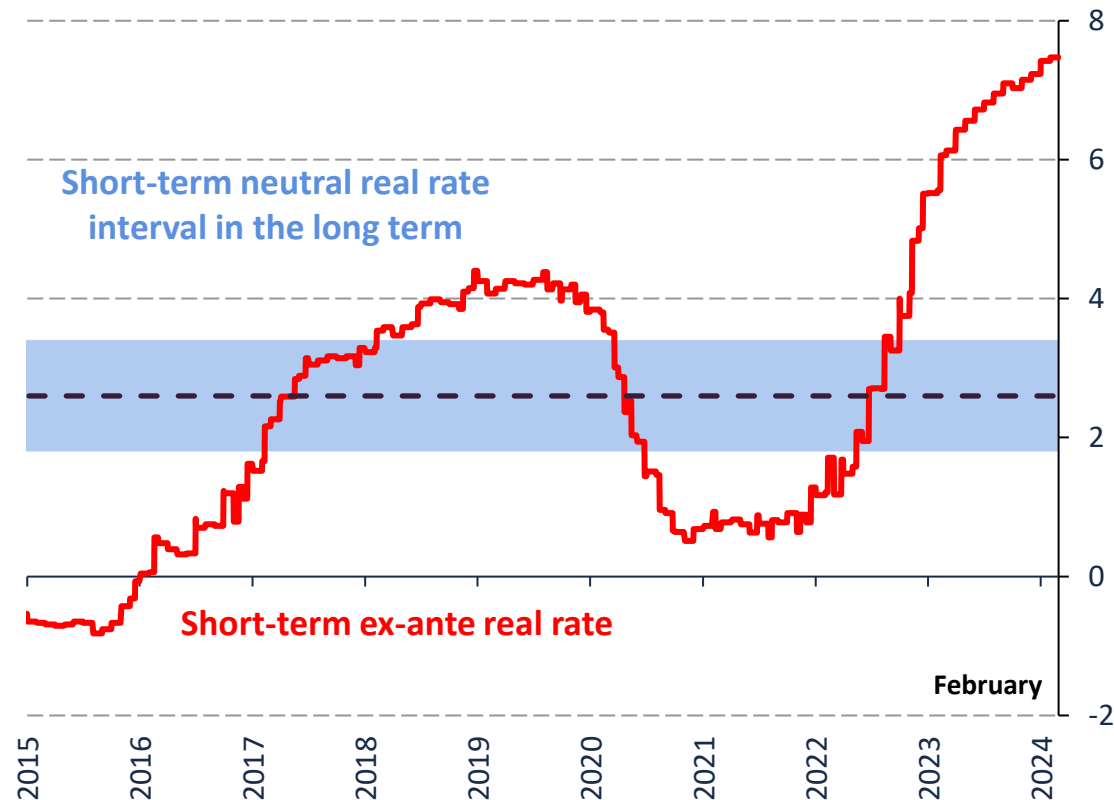
Considering that the reference rate was left unchanged and that inflation expectations adjusted downwards, the ex-ante real interest rate increased once again in the reported period and remained in restrictive territory.

Mean of 12-month inflation expectations
%



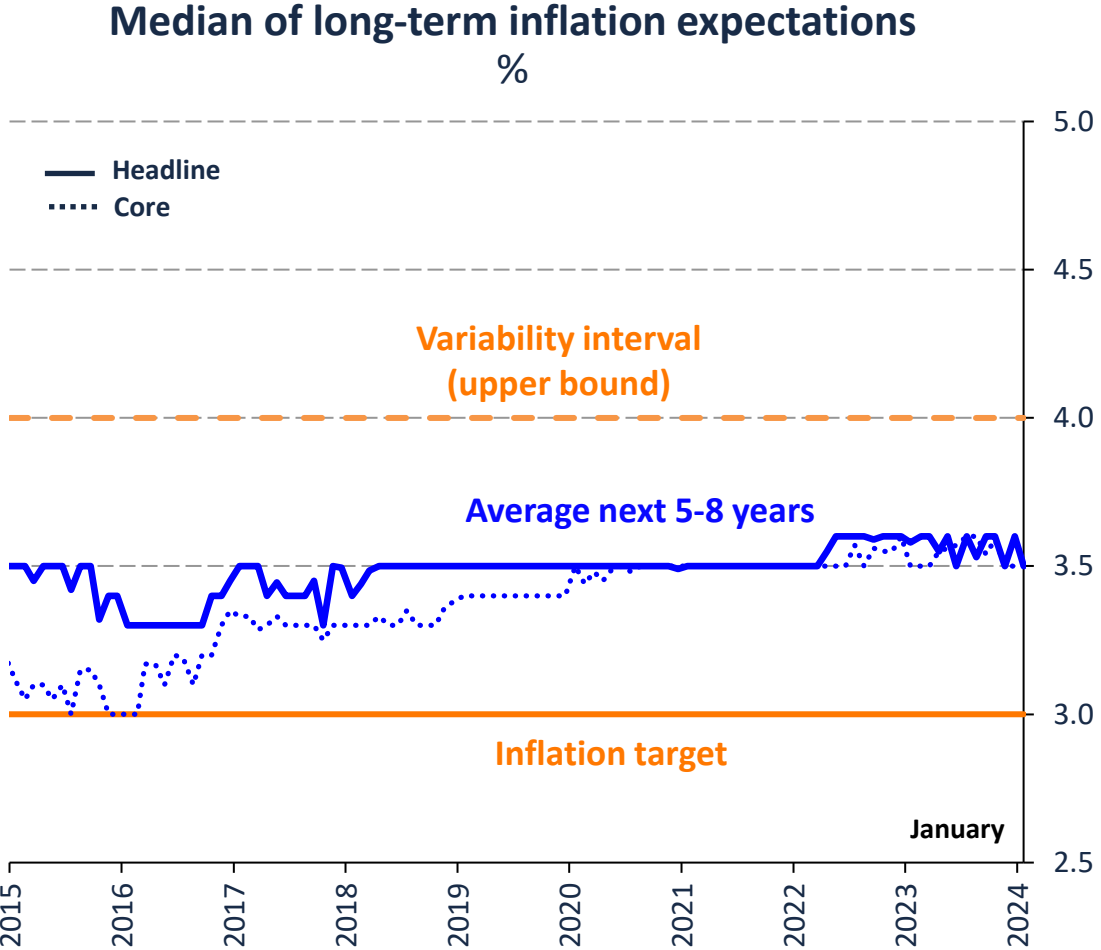
Note: Expected inflation for the next 12 months is shown.
Source: Banco de México's Survey of Private Sector Forecasters.

Short-term ex-ante real rate and estimated interval for the short-term neutral real rate in the long term^{1/}
Annual %



^{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 3.4%. The shaded area corresponds to the estimated interval for the short-term neutral rate in the long term. Source: Banco de México.

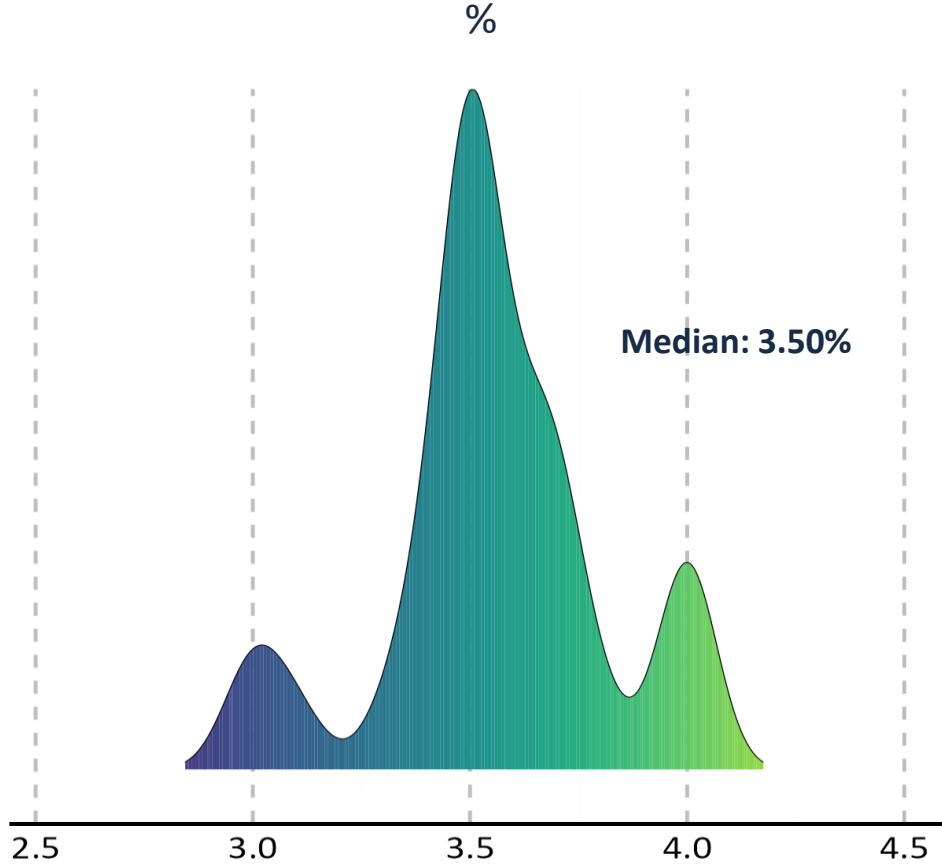
In the current inflationary episode characterized by significant shocks, the monetary policy stance has contributed to maintain long-term inflation expectations anchored.



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

Distribution of average headline inflation expectations for the next 5-8 years in January 2024

%

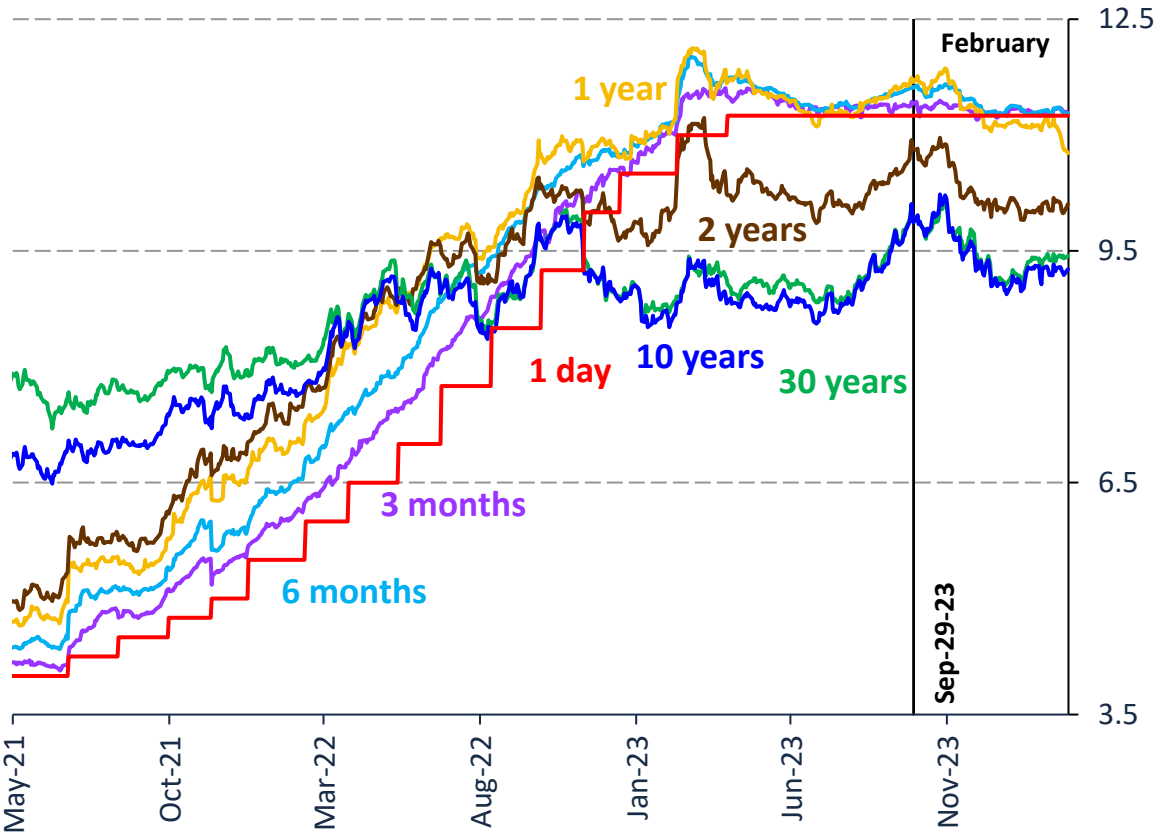


Source: Banco de México's Survey of Private Sector Forecasters. The reported figures correspond to the survey published on February 1, 2024.

During the reported period, interest rates on government securities declined along the entire yield curve, with more pronounced decreases in medium- and long-term interest rates.

Target for the overnight interbank interest rate and interest rates on government securities

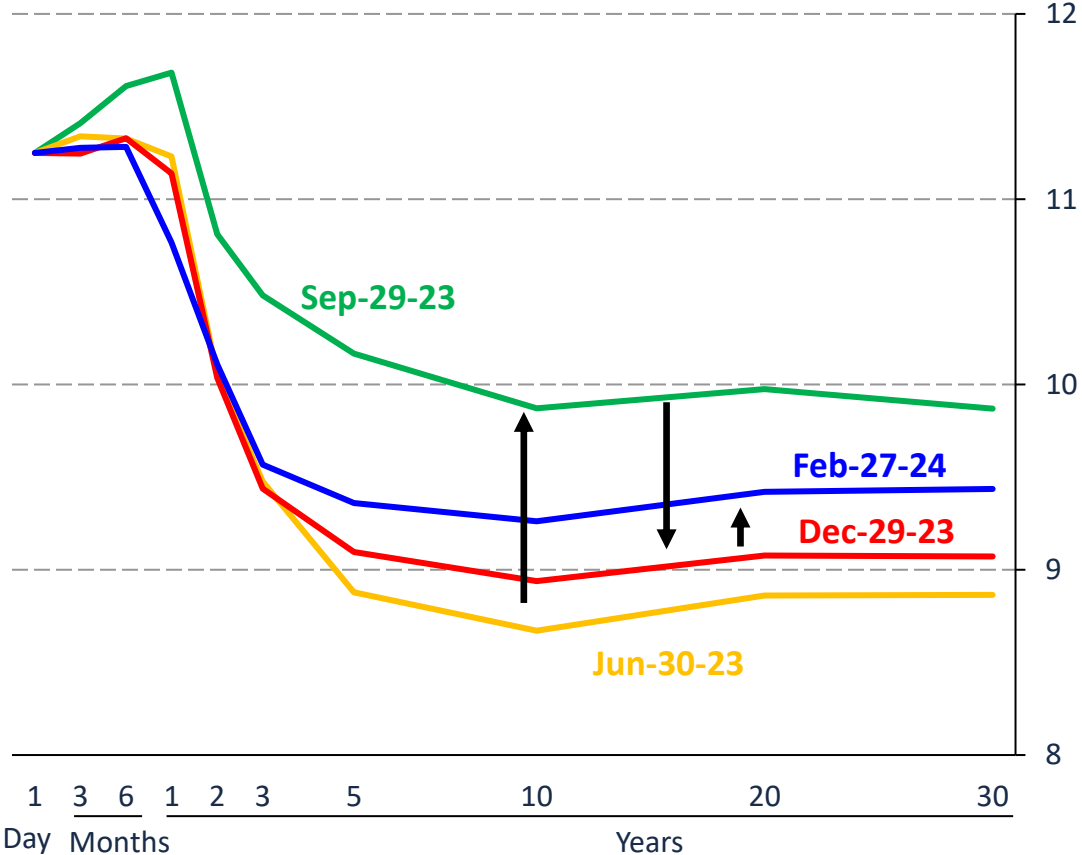
%



Source: Proveedor Integral de Precios (PiP).

Yield curve of Mexican government bonds

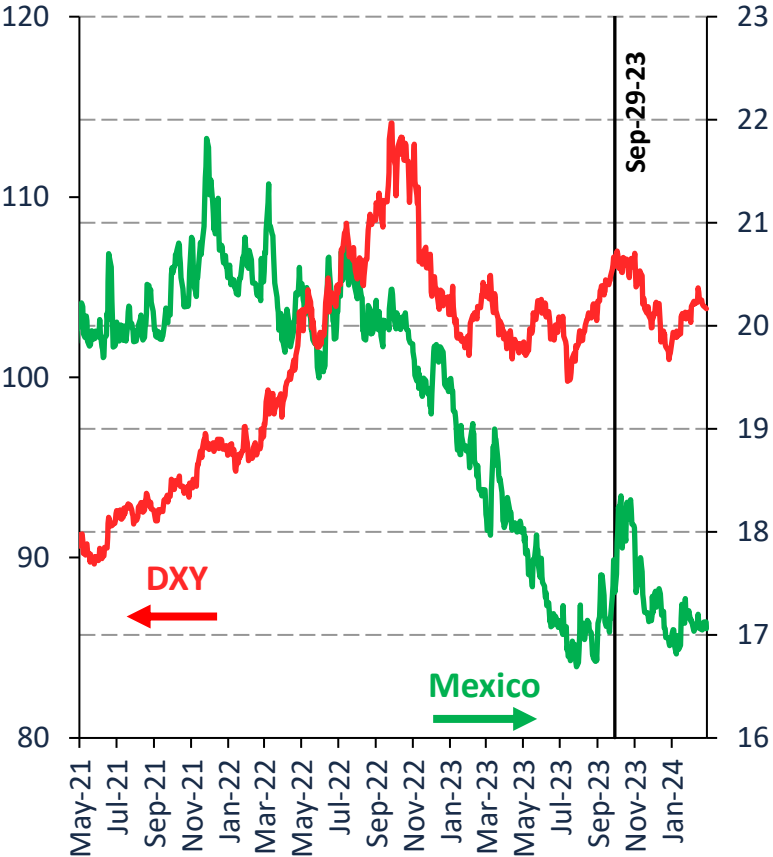
%



Source: Proveedor Integral de Precios (PiP).

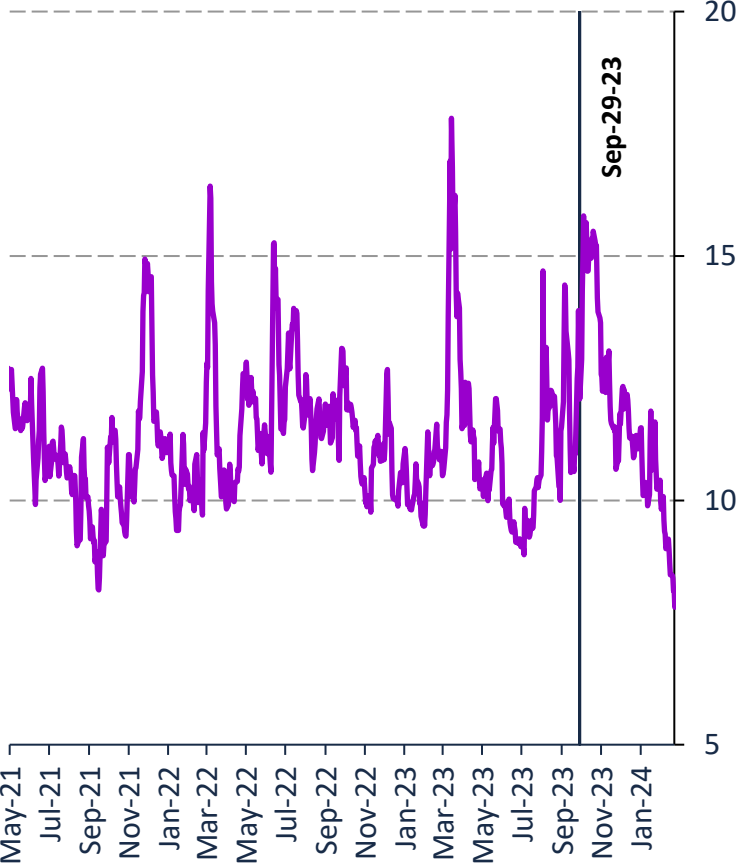
During the period covered in this Report, the Mexican peso appreciated in an environment of lower volatility in financial markets.

Nominal exchange rate and DXY ^{1/}
Pesos per USD, no units



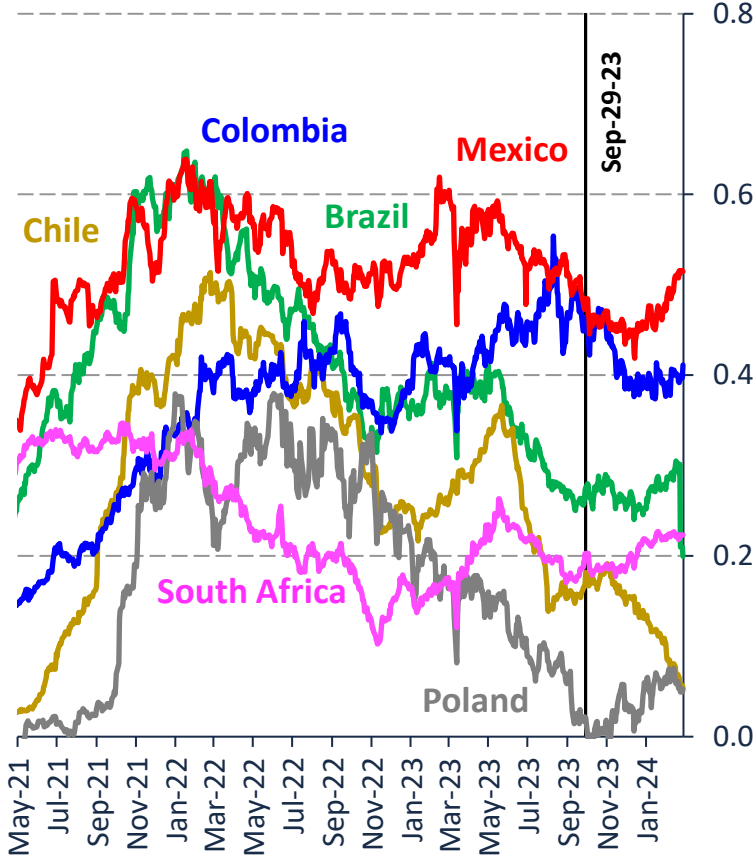
Note: The latest figure is as of February 27, 2024. 1/ The observed rate is the daily FIX exchange rate. For the DXY Index, an increase represents an appreciation of the US dollar. Source: Banco de México and Bloomberg.

Exchange rate volatility in Mexico's financial markets ^{2/}
%



Note: The latest figure is as of February 27, 2024. 2/ Refers to the implied volatility of 1--month options on the Mexican peso. Source: Bloomberg.

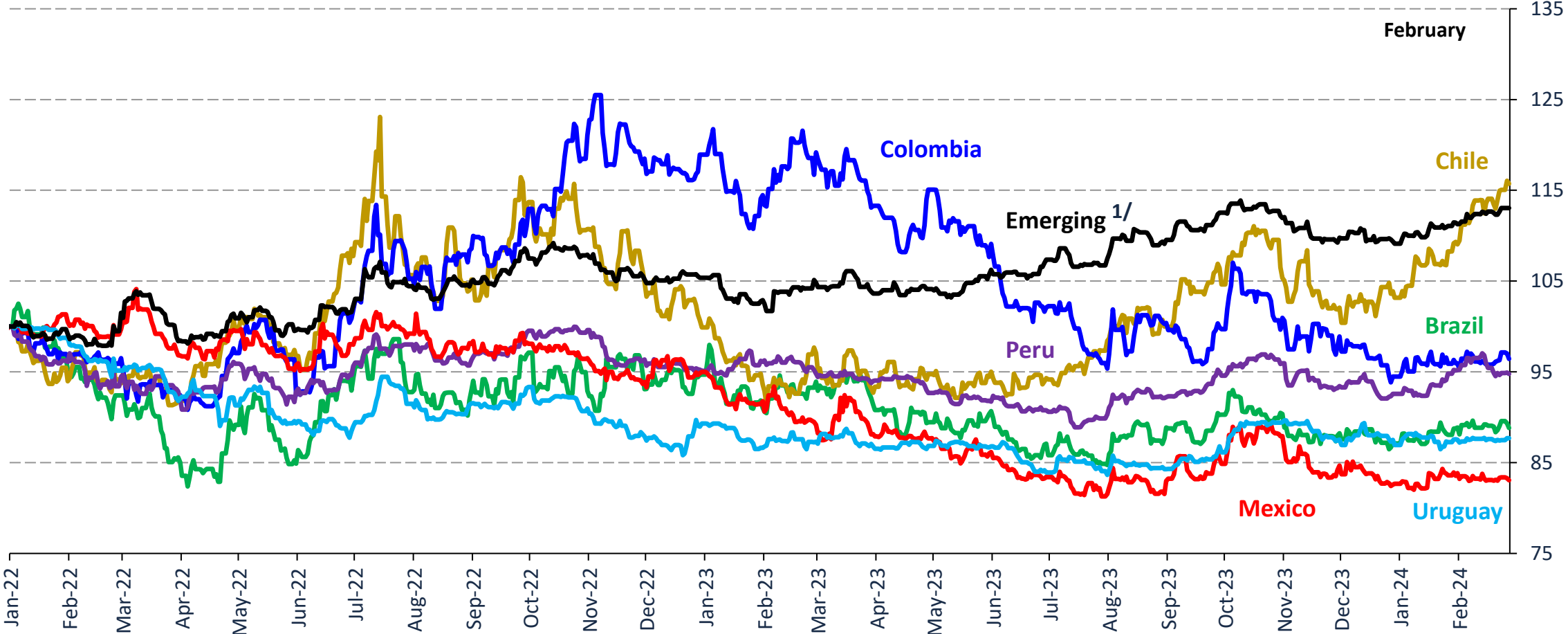
Volatility-adjusted spreads between emerging markets 1-year interest rates and those of the U.S. ^{3/}
No units



Note: The latest figure is as of February 27, 2024. 3/ The spreads are calculated with the implied spread in 1-year foreign exchange forwards, adjusted by implied volatility of the same time span. Source: Banco de México with Bloomberg data.

The Mexican peso continued to stand out as one of the most resilient currencies among emerging economies.

Exchange rate against the US dollar
Index Jan-01-2022=100



1/ Refers to the JP Morgan Emerging Market Currency Index (EMCI) Fixing.
Source: Bloomberg.

Contents

1 External conditions

2 Current situation of the Mexican economy

3 Inflation

4 Monetary policy

5 Forecasts and final remarks

Economic activity outlook

GDP growth ^{1/} Annual %

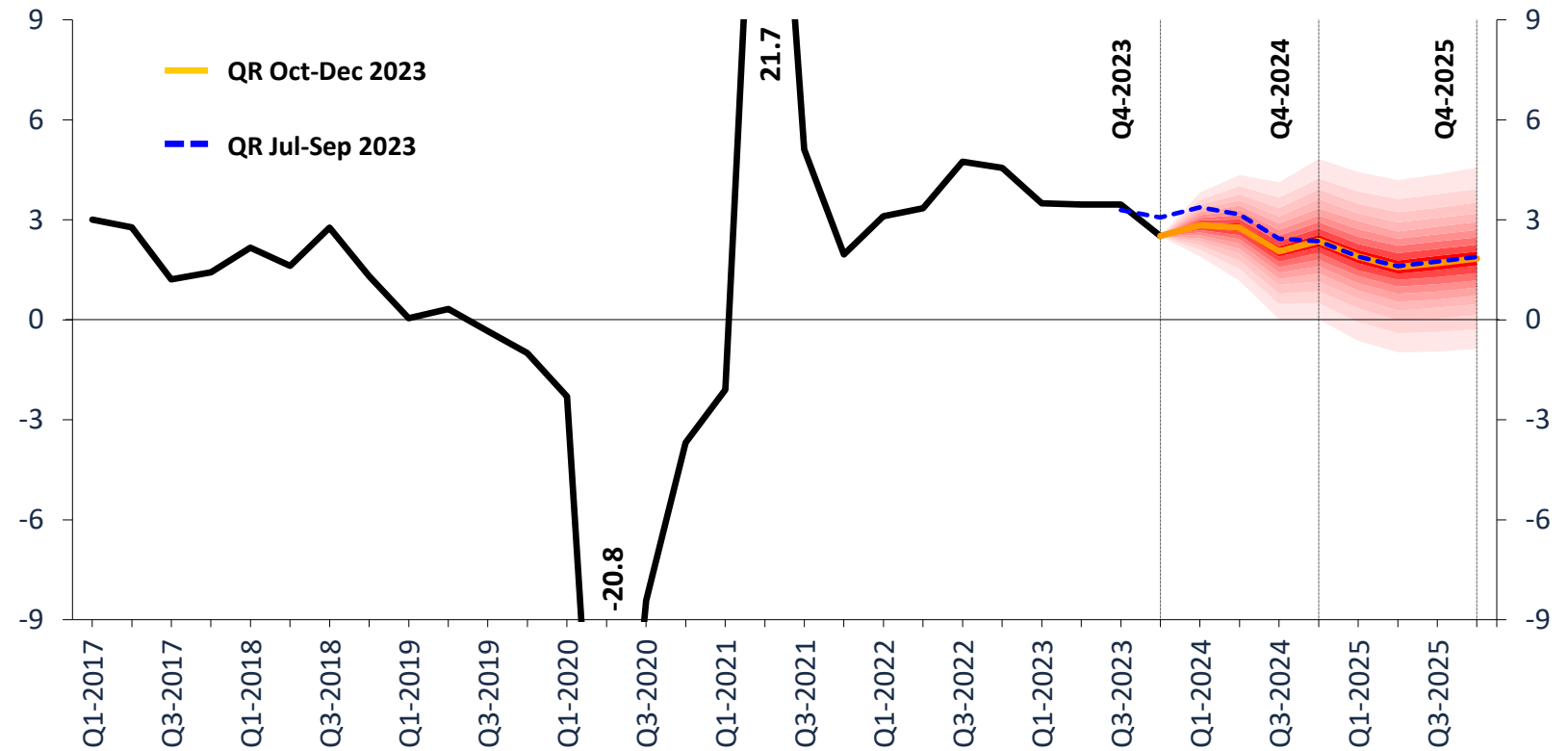
QR October - December 2023

Year	Point	Interval
2024	2.8	2.2 a 3.4
2025	1.5	0.7 a 2.3

QR July - September 2023

Year	Point	Interval
2024	3.0	2.3 a 3.7
2025	1.5	0.7 a 2.3

Fan Chart GDP ^{2/} Annual %, s. a.

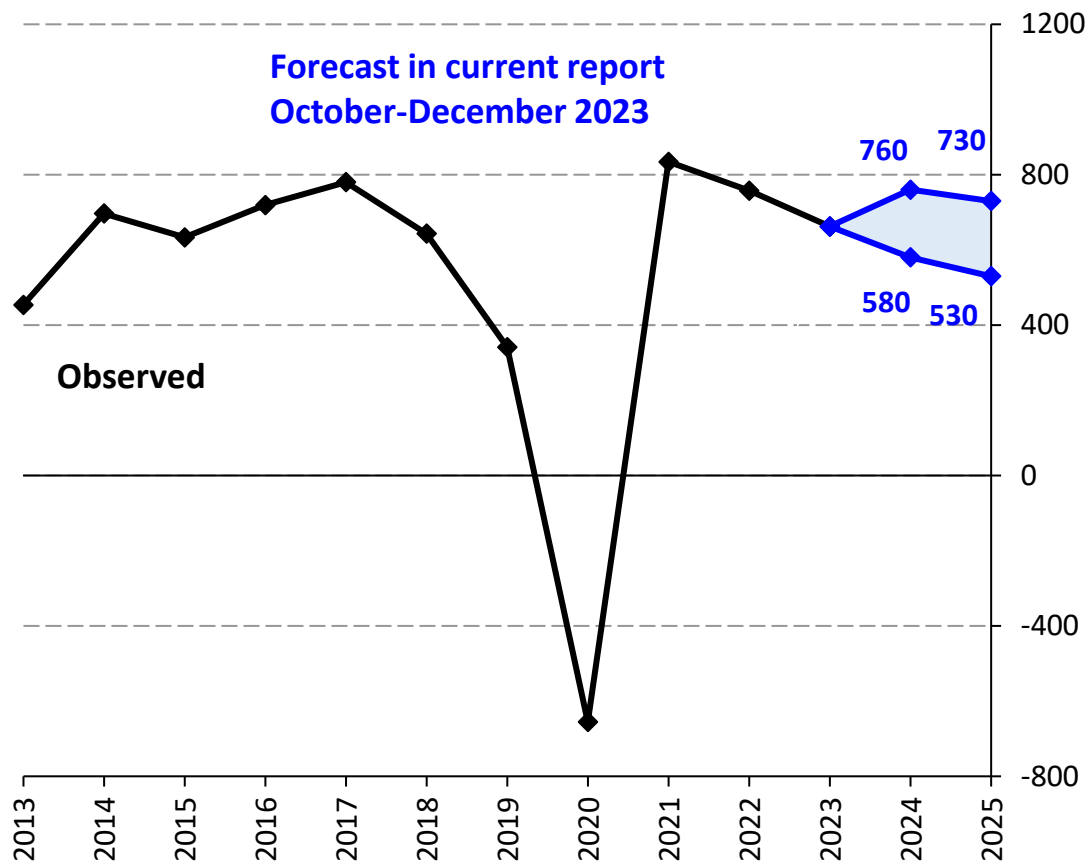


1/ Forecasts with figures without seasonal adjustment. Mexico's GDP growth in 2023 was 3.2% with non-seasonally adjusted figures. 2/ In the central scenario of the current Quarterly Report, the forecast starts in Q1-2024. In the past Quarterly Report, the forecast began in Q4-2023. Source: Banco de México.

Economic activity outlook

Increase in number of IMSS-insured jobs

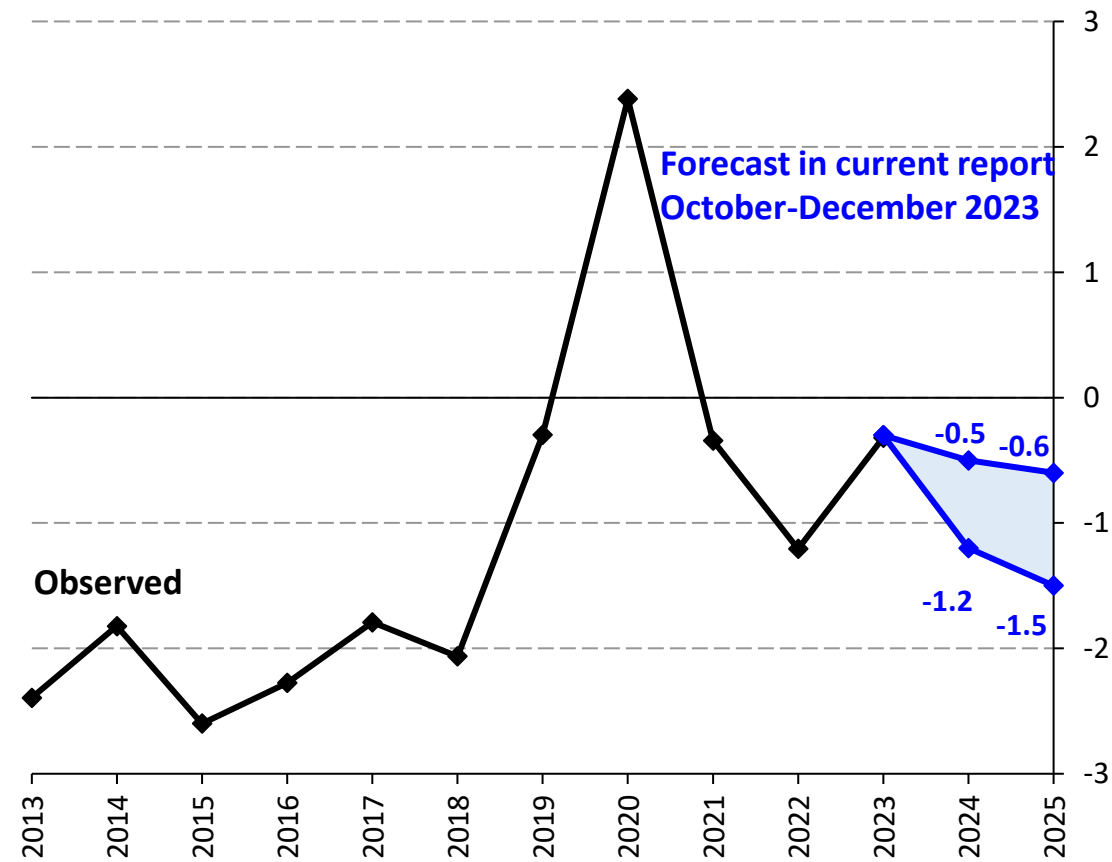
Thousands



Source: IMSS and Banco de México.

Current account

% of GDP



Source: Banco de México.

Risks to growth

Risks to growth of economic activity remain balanced.

To the downside

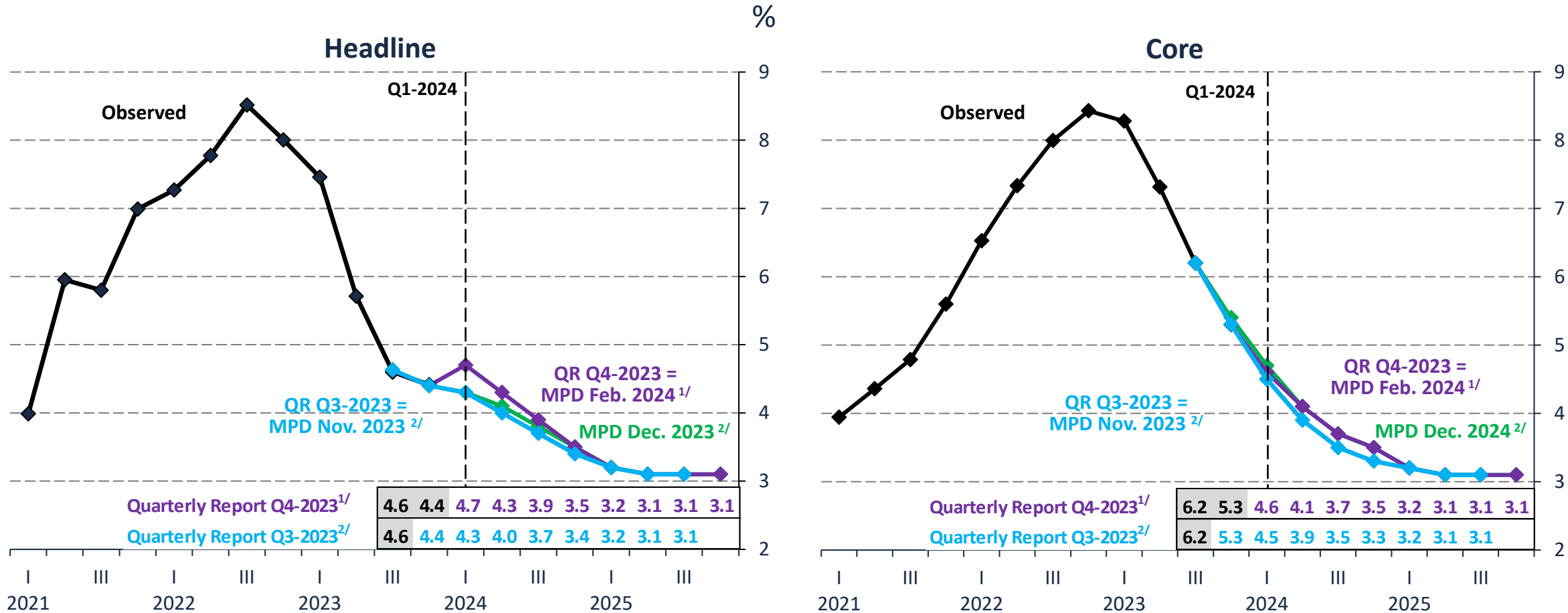
- I.** A lower external demand, particularly in the United States.
- II.** An escalation of several geopolitical conflicts.
- III.** Tighter financial conditions and/or episodes of volatility in financial markets.
- IV.** That public spending provides a lower-than-expected boost to economic activity.
- V.** Lower-than-expected recovery of investment spending.
- VI.** That weather phenomena affect national economic activity adversely.

To the upside

- I.** That growth of the US economy is greater than expected.
- II.** That the Mexican economy shows greater resilience than anticipated.
- III.** That, within the USMCA framework, the global reconfiguration of production processes provides a greater-than-expected boost to investment.
- IV.** That public spending results in a higher-than-anticipated boost to economic activity.

Headline and core inflation are still expected to continue decreasing, albeit more gradually in 2024 than estimated in the previous Report. The forecast that headline inflation will converge to the target in Q2-2025 and that core inflation will be close to 3% in that same quarter is maintained.

Annual inflation forecasts



Source: INEGI for annual variation observed data and Banco de México for forecasts. 1/ Forecast since February 2024. It corresponds to the forecast published in the Monetary Policy Statement of February 8, 2024. 2/ Forecast since December 2023. Corresponds to the forecast published in the Monetary Policy Statement of December 14, 2023.

Risks to inflation within the forecast horizon

The balance of risks for the trajectory foreseen for inflation within the forecast horizon remains biased to the upside.

To the upside

- I. Persistence of core inflation at high levels.
- II. Episodes of exchange rate depreciation.
- III. Higher cost-related pressures that could be passed on to consumer prices.
- IV. Greater-than-expected resilience of the economy.
- V. Climate-related shocks that could exert pressure on energy and on agricultural and livestock products' prices.
- VI. An escalation of different geopolitical conflicts.

To the downside

- I. A lower-than-anticipated economic activity.
- II. A lower pass-through of some cost-related pressures.
- III. That the lowest exchange rate levels with respect to 2023 contribute more than anticipated to mitigate certain pressures on inflation.

Final remarks

- Although the Mexican economy is expected to exhibit a high growth rate, supported by domestic spending, the announced fiscal policy stance, and, to a lesser extent, by the reconfiguration of global value chains, the year 2024 will continue posing different challenges. In this context, it is essential to **maintain sound macroeconomic fundamentals**, including fiscal discipline, a **monetary policy** focused on **price stability**, a healthy financial system, a well-capitalized banking sector, sustainable external accounts, and a flexible exchange rate.
- In this regard, **Banco de México's Governing Board** will continue setting its **monetary policy stance** with the strong commitment to foster an orderly **adjustment** of relative prices that leads **inflation to its 3% target** and ensures the **anchoring of inflation expectations**.
- To strengthen its domestic market and capitalize on the potential opportunities associated with trade openness, Mexico must continue adopting **measures that boost productivity** and ensure the efficient allocation of resources in the economy. The above would not only contribute to better prepare Mexico's economy to **face any adverse shocks** that may arise but would also establish solid foundations to achieve **greater economic growth** in a sustainable manner. All this would result in a stronger development of the national economy and, ultimately, in a greater **well-being of the Mexican population**.

Annex – Boxes

- 1** Effect of oil price shocks on US and euro area consumer price indices
- 2** Indicator of non-employed population that can potentially become employed
- 3** Recent evolution of bank financing to the private sector in different economies
- 4** Response of Mexican financial markets to US monetary policy statements



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