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Latam Daily: Mexico Growth Cools in June; Banxico Expected to Hike 75bps in September

- **Mexico: Minutes suggest a 75 bps hike in September while June GDP proxy suggests growth is cooling from a solid pace earlier this year**

MEXICO: MINUTES SUGGEST A 75 BPS HIKE IN SEPTEMBER WHILE JUNE GDP PROXY SUGGESTS GROWTH IS COOLING FROM A SOLID PACE EARLIER THIS YEAR

I. Banxico Minutes Suggest a 75 bps Hike in September

Banxico released the minutes of its August decision, where in a unanimous decision, the bank decided to increase the monetary policy rate for the second time by 75 basis points to 8.50%. In our view, the communiqué of the decision hinted that the Board might not opt for 75 bps again in September and now, after the discussion embodied in the minutes, we expect a divided Board in the next decision: on the one hand, further tightening seems unnecessary as some of the pressures outside the scope of central banks' action start to ease. On the other hand, we cannot ignore certain signals that indicate a process of de-anchoring inflation expectations (nominal wage increases at historical highs, deterioration of long-term inflation expectations). Therefore, in this uncertain environment and with a balance of risks, both local and external, markedly biased to the upside, **we expect Banxico to opt for another 75-bps hike in September.**

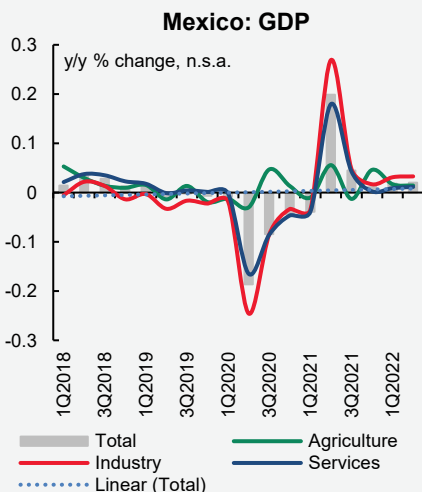
In the **global environment**, most agreed that global economic activity has continued to weaken: slowdown in China, the geopolitical conflict, prolonged inflationary pressures and tightening global financial and monetary conditions have increased fears of a recession in the near future. Some highlighted the case of the United States, where GDP fell for two consecutive quarters with labour market conditions remain strong. Even so, considerable risks to global growth remain.

Regarding **economic activity in Mexico**, most agreed that the recovery continues, supported by industrial production and services, although it remains incomplete and uneven. In this regard, several mentioned that certain indicators suggest that consumption has begun to decelerate, despite wage increases and remittances. Towards the second half of the year, the slowdown in the U.S. economy, the drought affecting several regions of the country and the lag in investment are factors that contribute to a downward bias in the balance of risks to growth.

On **inflation**, the majority highlighted that it is the result of external global factors that directly affect production and input costs, although another member mentioned insecurity in the country as another factor contributing to the increase in prices. However, what stands out most in the document is the discussion around the continuous increase in inflation expectations and the actions needed to avoid further deterioration in price formation. One board member sees the need to “continue the pace of tightening the monetary stance”, while another believes that “there are indications that we are close to reaching an unnecessarily high level of monetary tightening”. While the tone of the minutes continues to be restrictive, it is also evident that at least one Board member is concerned about tightening more than necessary, so while we expect Banxico to continue to act with the same “forcefulness” that we have seen in the last two decisions, **we cannot rule out the possibility that it will reduce the pace of tightening.**

—Luisa Valle

Chart 1



Sources: Scotiabank Economics, INEGI.

II. GDP in Q2-2022 increased owing to dynamism in both services and industry, but monthly proxy in June suggests downside risks

INEGI released the revised GDP figures for Q2-2022, which came in at 2.0% y/y in real terms, marginally below the flash estimate of 2.1% and in line with consensus (chart 1).

By sector, industry accelerated to 3.3% y/y (versus 3.0% previously), driven by the increase in manufactures, which accelerated 5.0% (from 4.7% previously). The services sector registered an increase of 1.2% y/y (from 1.9% previously), with important advances in most of its components, although lagged by a significant drop in corporate services owing to the effect of the outsourcing bill implement in April 2021. Services related to hospitality, and leisure activities continued to surge on a yearly basis as COVID-19-related risk almost dissipate (63% y/y and 24% y/y, respectively). The primary sector decelerated to 1.4% y/y, from 1.9% previously. With this, GDP grew 1.9% YTD during the first half of 2022 (table 1). In its seasonally adjusted quarterly comparison, GDP moderated to 0.92% q/q, from 1.14% previously. By sector, industry moderated by 0.86% q/q (1.39% previously), services sector also cooled 0.92% q/q (1.39% previously) and the primary sector rebounded 0.94% (-1.81% previously).

In June alone, the GDP proxy (IGAE), also released by INEGI, dropped for the second consecutive time on a seasonally adjusted monthly basis (chart 2), this time from -0.2%

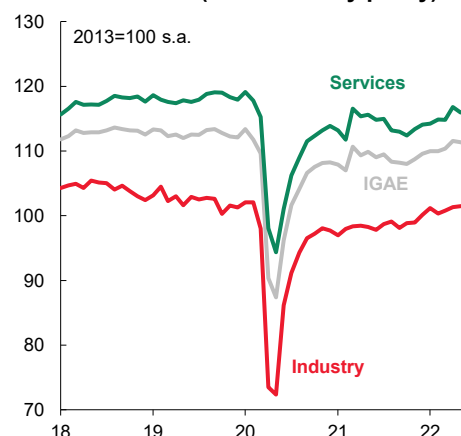
to -0.3% m/m. Industry moderated from 0.2% to 0.1% m/m, while services showed no change (0.0% m/m from -0.7% previously), and primary activities fell -6.6% m/m from 2.0% previously. In its annual comparison nsa, the IGAE index moderated from 2.1% to 1.6% y/y.

Looking ahead, we expect modest advances during the remainder of the year, as we anticipate a 1.7% GDP growth during 2022, and 1.5% for 2023, in line with the expected slowdown in the US economy, and the effect of interest rate hikes.

—Miguel Saldaña

Chart 2

Mexico: IGAE (GDP monthly proxy)



Sources: Scotiabank Economics, INEGI.

Table 1: Mexico—Gross Domestic Product (GDP)

GDP	% Share of GDP	Annual % Change, NSA					Quarterly % Change, SA		
		2Q2021	3Q2021	4Q2021	1Q2022	2Q2022	1Q2022	2Q2022	
GDP	100.0	19.9	4.5	1.1	1.8	2.0	1.1	0.9	
Primary sector	3.4	5.6	-1.3	4.6	1.7	1.4	-1.8	0.9	
Industrial activity	28.6	26.9	4.8	1.7	3.1	3.3	1.4	0.9	
Mining	4.7	6.3	2.2	1.1	2.3	0.1	1.7	-1.1	
Utilities	1.5	5.2	-1.9	-1.0	2.2	3.7	2.0	1.5	
Construction	5.9	29.5	9.8	1.9	0.0	1.1	0.4	1.3	
Manufacturing	16.5	36.5	4.5	2.1	4.7	5.0	1.6	1.1	
Services	63.7	18.0	4.3	0.3	0.9	1.2	1.4	0.9	
Wholesale trade	8.9	25.1	10.8	5.7	6.0	7.7	2.4	1.9	
Retail trade	9.4	39.8	8.9	4.1	4.1	6.3	-0.3	4.0	
Transport & storage	7.0	53.8	19.2	14.9	16.6	14.3	3.8	4.0	
Information & communication	3.6	7.9	9.0	5.0	15.2	11.0	3.3	4.7	
Financial & insurance	4.5	-2.1	-1.6	-1.9	1.4	1.0	2.5	0.8	
Real state	11.9	4.2	3.2	2.3	2.2	3.2	0.7	1.2	
Professional & scientific	2.1	11.3	4.7	3.9	0.2	6.3	0.9	6.0	
Corporate	0.7	3.5	3.2	3.8	6.8	11.0	0.3	2.8	
Business support	1.1	14.5	-48.1	-70.3	-73.6	-73.6	-3.4	-0.5	
Education	3.7	-0.2	-0.1	0.7	3.0	0.5	1.0	-0.4	
Health	2.4	15.3	7.9	4.0	4.0	5.0	2.4	4.1	
Recreational	0.6	249.9	71.2	40.1	62.8	63.2	18.2	16.1	
Accommodation & restaurant	2.2	172.9	68.1	45.7	42.7	24.8	4.3	4.1	
Others	1.6	10.2	8.9	5.6	4.8	0.9	0.2	-2.5	
Government	3.9	2.2	0.3	0.4	-0.4	-2.6	-0.2	-0.8	

Sources: Scotiabank Economics, INEGI.

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