

FX Daily: Cautious Banxico rate cut to keep Mexican peso supported

We're expecting a quarter point rate cut in Mexico today. But the policy guidance should remain cautious and we think the peso will continue to outperform its peers



📈 USD: Good day for the dollar ahead

With the reported cases of coronavirus rising, risk assets should be on the back foot today, with the US dollar outperforming most of its G10 peers (bar the Japanese yen). Commodity currencies should be the laggards (see [Coronavirus: Gauging the market fallout for detailed analysis](#)). In the G10 FX space, the Norwegian krone and Australian dollar screen vulnerable, while in the emerging markets space, the rouble and South African rand should underperform today. On the US data front, the focus turns to US January CPI. January headline CPI will largely be determined by the core rate, which should bounce back a touch after a surprisingly soft 0.1% month-on-month reading in December. Markets are likely to overlook this report as the CPI readings for February are going to be softer due to energy, the stronger dollar and other commodity (metal) weakness.

➡ EUR: Lower and lower

EUR/USD continues to dip lower (breaking below the 1.0880 support level) and we don't see any

reason for a change in the trend. Renewed concern about the coronavirus and its implications for Chinese growth are EUR/USD negative given the openness of the eurozone economy.

↑ HUF: Peaking inflation to provide some respite to HUF

While we look for another increase in Hungarian January CPI today (4.5% from 4.0% previously) we see January as the peak for prices this year and expect inflation to fall sharply to 3.1% year-on-year by May. The improving CPI dynamics (with CPI returning fast towards the 3% target) should ease pressure on the oversold Hungarian forint, which has been one of the main EM underperformers so far this year (only surpassed by the Brazilian real and South African rand). With EUR/HUF reaching an all-time high of 340 yesterday, we look for a positioning driven reversal to 335 in coming weeks.

➔ MXN: Cautious Banxico cut to keep MXN real rate advantage in place

The growing slack in economic activity and the strong Mexican peso performance should tip the balance in favour of another 25 basis point rate cut by Banxico today ([see Banxico Preview](#)). Concerns over core inflation and especially rising wages suggest, however, that monetary policy guidance should remain cautious, but our bias is for a deeper cycle than currently expected. The widely-expected cut and the cautious guidance means that MXN should continue to enjoy one of the highest real rates in the EM space. Coupled with a significant improvement in Mexico's trade surplus in recent quarters, MXN should continue to outperform vs its peers.

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