

Contributors

Juan Manuel Herrera

Senior Economist/Strategist
Scotiabank GBM
+44.207.826.5654
juanmanuel.herrera@scotiabank.com

Guillermo Arbe, Head Economist, Peru
+51.1.211.6052 (Peru)
guillermo.arbe@scotiabank.com.pe

Sergio Olarte, Head Economist, Colombia
+57.601.745.6300 Ext. 9166 (Colombia)
sergio.olarte@scotiabankcolpatria.com

Jorge Selaive, Head Economist, Chile
+56.2.2619.5435 (Chile)
jorge.selaive@scotiabank.cl

Eduardo Suárez, VP, Latin America Economics
+52.55.9179.5174 (Mexico)
esuarezm@scotiabank.com.mx

Latam Daily: Mexican CPI to Make or Break August Cut?

Overnight markets are trading with a risk off mood with broad-based losses in currencies outside of the havens (JPY and CHF) that follow melting US equity futures on poor after-hours earnings releases (namely in tech). European bourses are taking a hit from the US mood but also from earnings disappointments at home. After a sharp 3.5% decline yesterday, WTI crude oil is picking up a small 0.5% gain while iron ore and copper trade 0.4% gains and losses, respectively.

USTs are bull steepening slightly, while EGBs and gilts are twist steepening, after German and Eurozone PMIs missed expectations and UK PMIs came in line with forecasts. A report that the BoJ's decision next week is closer to call than markets believe and that officials will announce a taper of bond purchases is weighing on the global long end at writing. The BoC's (likely) rate cut and US PMIs, both at 9.45ET, await as the main events on today's G10 calendar.

With the risk-negative tone, the MXN sits at the bottom of the majors' leaderboard on a 0.5/6% loss that takes the cross to the 18.25 pesos area, a zone that it hasn't seen since early-July. It could be that the unwinding of global carry trades amid JPY strength is dragging on the MXN at the same time as US election uncertainty and weak global growth prospects (namely out of China), while soft Mexican economic activity data injects some uncertainty into Banxico's decision in August.

Today's 8ET release of Mexican H1-Jul CPI is a key make or break release for whether Banxico lowers its overnight rate at its meeting two weeks from now. The recent losses in the MXN (and the uncertain horizon for the currency) and the uptick in local inflation in 2024 (even if mainly due to food and energy inflation) would support a more cautious rate hold stance. On the other hand, weakening growth (at home and abroad), so-far relatively well behaved core inflation, and Fed cuts on the horizon would augur a cut. It's a tough call, and markets are undecided with about 11bps in cuts implied.

For today's release, an inline bi-weekly inflation reading of 5.4% y/y and a 4.0% core print is unlikely to reduce uncertainty for markets, and may even reduce cut odds slightly given the shock of a near mid-5s headline print this far into Banxico's restrictive cycle. It would not rule a cut out, however, and other variables like the MXN or international political and market developments could very easily motivate easing. With some luck, core CPI could register a 3-handled reading today (high 3s, of course) that would lift cut bets above toss-up odds. The five-member Banxico board has a more dovish than neutral bias to it, and we think that three officials will find sufficient evidence in a soft-ish core CPI print to lower rates in August.

—Juan Manuel Herrera

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