



Mexico

After the MXN's large devaluation in the midst of the 1994 crisis, Mexican authorities switched from the currency's regime from a managed exchange rate to a free float. To retain some control over the Peso, representatives of Banxico and the Finance Ministry who comprise the Exchange Commission (EC) set several rule-based intervention schemes aimed at managing reserve accumulation and abating volatility. USD/MXN options-based interventions began in August of 1996. In February of 1997, spot purchases were added as an intervention tool to inject USD liquidity during periods of market stress so as to combat volatility. Both of these intervention programs were canceled on June of 2001 after being employed a combined total of 14 times. The interventions occurred mainly between August of 1998 and January of 1999 and the total amount of USD injected into the FX market was USD 1.95bn.

Starting on May of 2003, the EC set USD auction mechanism to manage the accumulation of reserves as higher and more volatile oil prices had become a threat to the MXN. Despite the auctions, reserves grew very quickly to a record high level of USD 87bn. The auctions were indefinitely suspended on July 21st 2008 after the USD/MXN fell to 9.85 during the first half of the year.

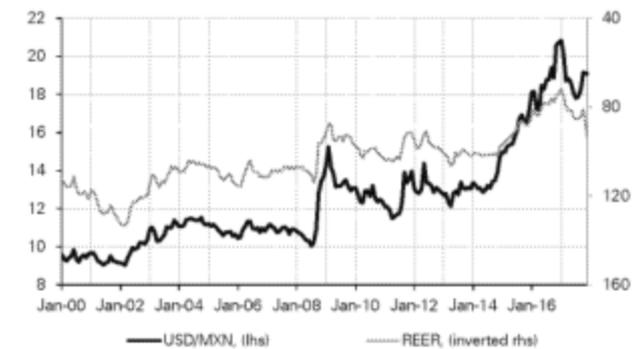
Yet after struggling to control the Peso's appreciation the tables turned and the currency experienced strong appreciation pressures in the midst of the 2008 crisis. The Mexican corporate sector suffered FX-related losses because of its exposure to derivatives risk pushing the demand for USD hedges even higher. The EC reacted by setting a rule-based intervention scheme via USD auctions similar to the one used in the 1990s. On days in which the USD/MXN increased by more than 2% relative to the previous closing, USD 400m would be offered. The rule was supplemented with an extra auction of USD 100m to be held every day (until October of 2009) regardless of price action and extra discretionary auctions on particularly volatile days.

During 2015, 10% of reserves were spent on interventions and the MXN remained weak. On November of 2015, the EC added conditions to its rules-based interventions: USD 200 mm would be sold on days of an MXN depreciation of at least 1% with an extra USD 200 mm offered if the depreciation was greater than 1.5%. Finally, on February 2016 the EC suspended all rules-based interventions when both the Ministry of Finance and Banxico announced a series of fiscal and monetary policy actions to improve Mexico's macroeconomic environment and more specifically its fiscal accounts. Banxico raised its policy rate by 50bps and since then it seems to have responded to brusque

MXN sell-offs with rate hikes despite the stability of inflation expectations, the negative output gap, and the little evidence of a relevant exchange rate pass-through.

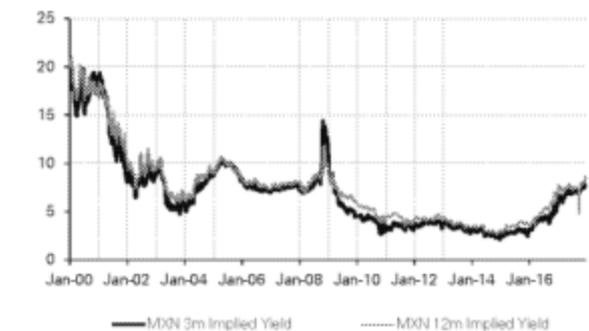
On February 2017 Mexico's Exchange Commission announced it would intervene the FX market by auctioning off domestic NDFs settled in MXN up to a notional amount of USD 20bn. As of December of 2017 only USD 5bn worth of the instrument had been issued.

USD/MXN spot and REER



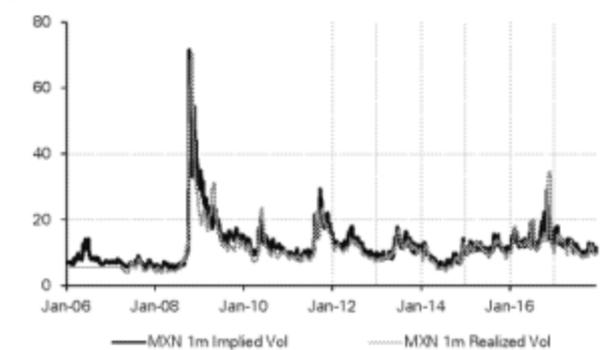
Source: Deutsche Bank, Bloomberg Finance LP

3M and 12M USD/MXN FX Forward implied yield



Source: Deutsche Bank, Bloomberg Finance LP

1M USD/MXN implied volatility and realized volatility



Source: Deutsche Bank, Bloomberg Finance LP