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Maybank

RMB Watch

Bears Not In Control Yet

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Watching Price Action and Key Levels

Key View:

- USDCNH touched record high of 7.1965 on Wed just before the US Secretary of State Pompeo declared that Hong Kong is no longer autonomous from China. **Eyes are on the upcoming news conference and Trump promised new policies on China.** Trump rarely keeps secrets well and the uncertainty there is also reflected in recent USDCNH moves.

- While the USDCNH move up this week to touch the record high of 7.1965 after we downgraded the RMB forecast should have been the early signs of vindication for us, we still like to eye certain levels. USDCNH has retraced lower since due to broader USD softness and stronger CNY fixes. While bullish momentum remains intact, further retracement back towards the 21-dma/50-dma could even form a rising wedge that typically precedes a bearish reversal, albeit a modest retracement of the recent rally. A drop below **7.1040 (50-dma)** would mean break-out to the downside.

- Month-end flows and stronger EUR might have weakened the USD this week. USDCNH bulls may be reinvigorated in Jun as US and China tensions escalate with potential sanctions to be imposed and counteractions anticipated. A clean break above 7.1965 is needed for USDCNH bulls to extend and for the ascending triangle to play out. That could bring the USDCNH beyond 7.30. Beyond the RMB, the shift of focus away from trade and tariffs could see less damage for regional currencies, excluding the RMB and KRW more affected via the sentiment channel at least for the next 1 to 3 months.

What We Watch:

- NBS PMI and Caixin PMI releases over 31st May - 3rd Jun.

- May trade data on 7th Jun.

- CPI on 10th Jun.

- Monetary policy on 10-15th Jun.

Trade deal Still in Place, Escalation Elsewhere

We downgraded our RMB forecast earlier this week, taking into consideration the risk premium as the US and China had showed little restrain in escalating tensions on many aspects. Amongst the hostile exchanges and actions that included 1) a bill passed by the US Senate that could see Chinese companies delist in the US stock exchanges and drove JD.com and Netease to apply to list on HKEX, 2) a bill passed by the Congress to impose sanctions on Chinese officials involved in the repression of Uighurs in Xinjiang and 3) curbing Huawei's ability to use US technology and equipment made overseas to manufacture semiconductors for their products; 4) the cancellation of plans (under the pressure of the White House) for the Federal Retirement Thrift Investment Board to invest in index funds that include Chinese shares; 5) threats of sanctions on officials, entities that enforce the new national security law enacted for Hong Kong by China along and above all 6) blaming China for the COVID-19 pandemic, **it would be easy to forget the fact that the US and China are still eager to keep phase 1 of the Trade Deal.** The two nations' trade negotiators were quick to have a phone call on 8 May (Asia morning) and came to the consensus that "both countries fully expect to meet their obligations under the agreement in a timely manner". China also reiterated its pledge to implement the phase 1 of the trade deal at the NPC earlier this week.

With the US Secretary of State Mike Pompeo declaring that **Hong Kong is no longer autonomous from China,** the Treasury Department could **impose controls on transactions and freeze assets of Chinese officials** and entities involved in enforcing a new national security law. Trump can also choose to **remove Hong Kong special trade status and subject the city to the same punitive tariffs and sanctions that mainland China bears.** Fox News also reported that the White House may restrict visas for students and researchers in China from studying in the US. In addition, we still await to see if the Trump administration can limit US investors' portfolio flows into China apart from effecting the U-turn on the Federal Retirement Thrift Investment Board plans.

More recently on 27th May, Trump has hinted to the press about his administration's work on "something now" that will be unveiled later in the week. He described the upcoming action to be "Very powerfully, I think.", "Very interesting". Trump also mentioned that Hong Kong is likely to "lose its financial industry" if "China takes over". The US Chamber of Commerce urged the White House to ensure a constructive relationship between the US and Hong Kong. Yesterday (28 May), **Trump told the press that he will announce new policies on China at the news conference tonight.** Trump rarely keeps secrets well and the uncertainty there is also reflected in the USDCNH moves.

Technical Analyses – Watching the price action and key Levels

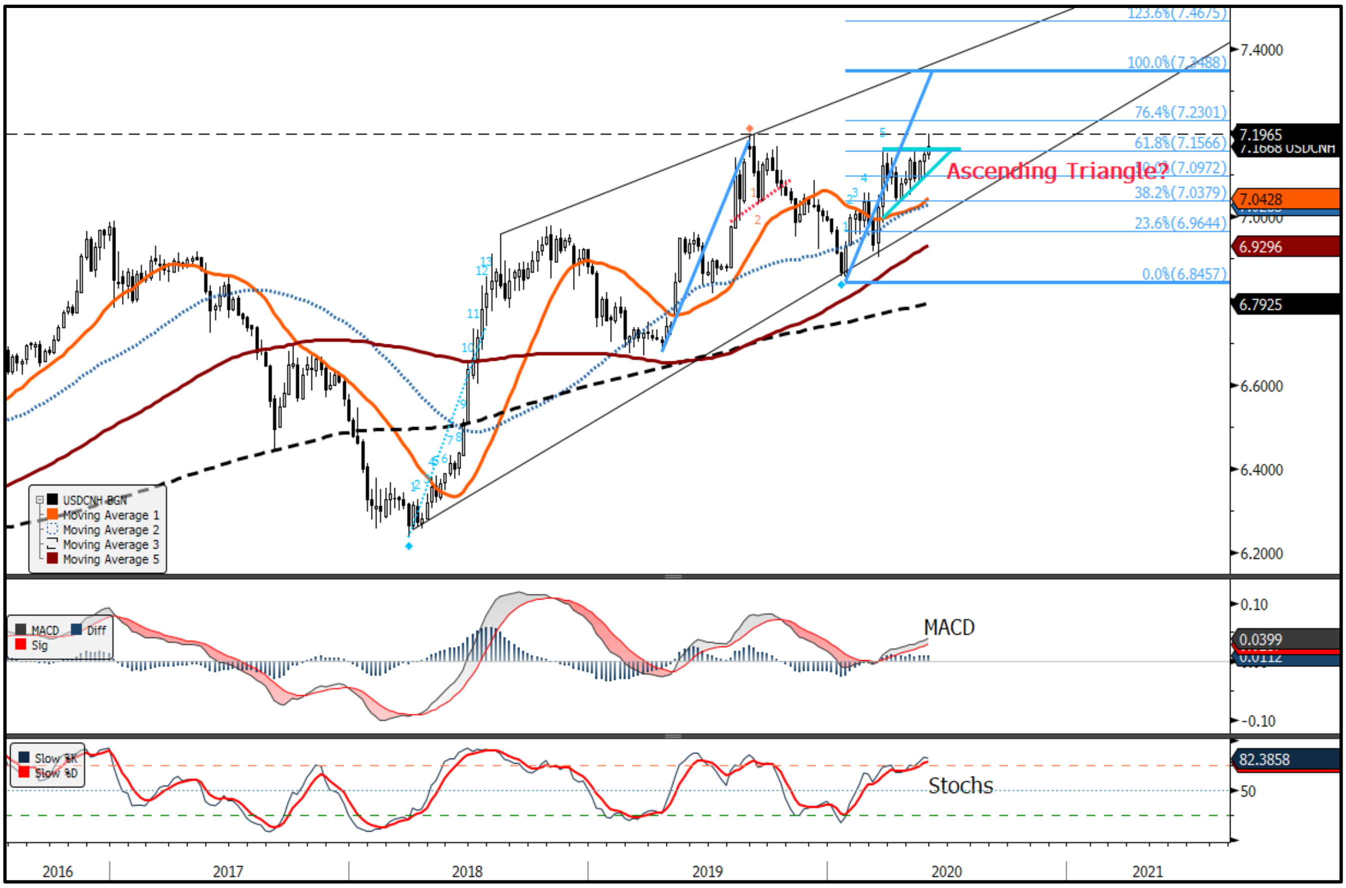
USDCNH spiked to touch the record high of 7.1965 right before Mike Pompeo made the declaration on Hong Kong's state of autonomy on Wed. However, PBoC was quick to increase the countercyclical factor to the USDCNY reference rate on Thu with the USDCNY fix deviating more than usual from the USDCNY estimates. With that, PBoC has cooled off bearish steam in the CNY for now.

USDCNH (Daily) – Some Bullish Momentum Intact

Source: Bloomberg, Maybank FX Research & Strategy

USDCNH spiked above the year high to touch the record high of 7.1965 after we sent out our note that downgraded the RMB forecast. This move should have been the early signs of vindication for us but we still like to eye certain levels. The bright blue lines marked the ascending triangle and it seems there was a breakout on Wed. With that, our call for it to head higher towards the 7.30-figure could play out. Momentum is still bullish for the pair to do so. However, the lack of follow through, helped not the least by the stronger than expected fix makes the price pattern less clear and the break-out of the ascending triangle has less conviction at this point. Further retracement back towards the 21-dma/50-dma could even form a rising wedge that typically precedes a bearish reversal, albeit a modest retracement of the recent rally. A drop below 7.1040 (50-dma) would mean break-out to the downside.

USDCNH (Weekly) - Needs a Clean Break of the 7.1965 for Bulls to Extend



Source: Bloomberg, Maybank FX Research & Strategy

The lack of follow through for USDCNH upmove was not just due to the USDCNY fix. Broadly, the USD was moving lower due to month-end flows and EUR gains. We may still see USDCNH bulls reinvigorated in Jun (after month-end). However, the clearance of the 7.1965 is key or this pair could have formed a double top bearish formation, marked by the black dashed-line. In that scenario, USDCNH would come crashing below the 7-figure. We are still of the view that risks are skewed to the upside for the USDCNH as bullish momentum is intact on the daily, weekly and monthly chart. In fact, MACD forest is rising gradually in the past few monthly candle sticks.

At this point, we also like to highlight how the USDCNH has been on the rise since the trade war 2018 and a broad rising wedge has since formed. As indicated by the Fibonacci extension (also indicated on our FX Insight - Familiar Headwinds for RMB), the current upmove may take the USDCNH towards the upper bound of the rising wedge before a potentially significant correction. MACD forest shows bearish divergence formed by the peaks of 2018 and 2019. This trend could continue for a third peak before a break-out of the rising wedge (bearish for USDCNH). That would be in line with our view for RMB to see weakness before strength. Weakness in the near-term as the US rushes to take action on China in the near-term to shore up political support ahead of the Presidential Election on 3rd Nov. According to the Gallup article, historically, all incumbents with a job approval rating of 50% or higher have won reelection, and presidents with approval ratings much lower than 50% have lost. Trump has approval ratings in the mid-to-upper 40% range. The recovery in the CNH could come towards the end of the year as the elected (or re-elected) US President may need to focus more on domestic issues and repairing the weakened economy. Potential breakthrough of the vaccine development may also lift consumer and business sentiment and give USDCNH a nudge lower, rejoining the rest of the USDAxJ.

Implications for other FX

Beyond the RMB, given that the escalation has shifted away from trade to sanctions and student visa restrictions, we see a different impact on non-RMB FX. The sentiment channel is not spared apparently - RMB and the KRW were more disproportionately affected while the rest of AxJ FX saw their earlier weakness in the week reversed. Market players remain vested in the Big picture –the reopening of economies and vaccine hopes - this is still keeping broad sentiment, US equities supported for now at least for the next 1-3 months.

So, in terms of broad FX plays, we prefer stay cautious but not defensive yet. We monitor any signs of US and China turning sour on trade or tariffs. A return to that could have more adverse ramification for AxJ FX.

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