

RMB Watch

Leaning Against A Strong Wind

Still Remain Short-Term Bearish on USDCNY

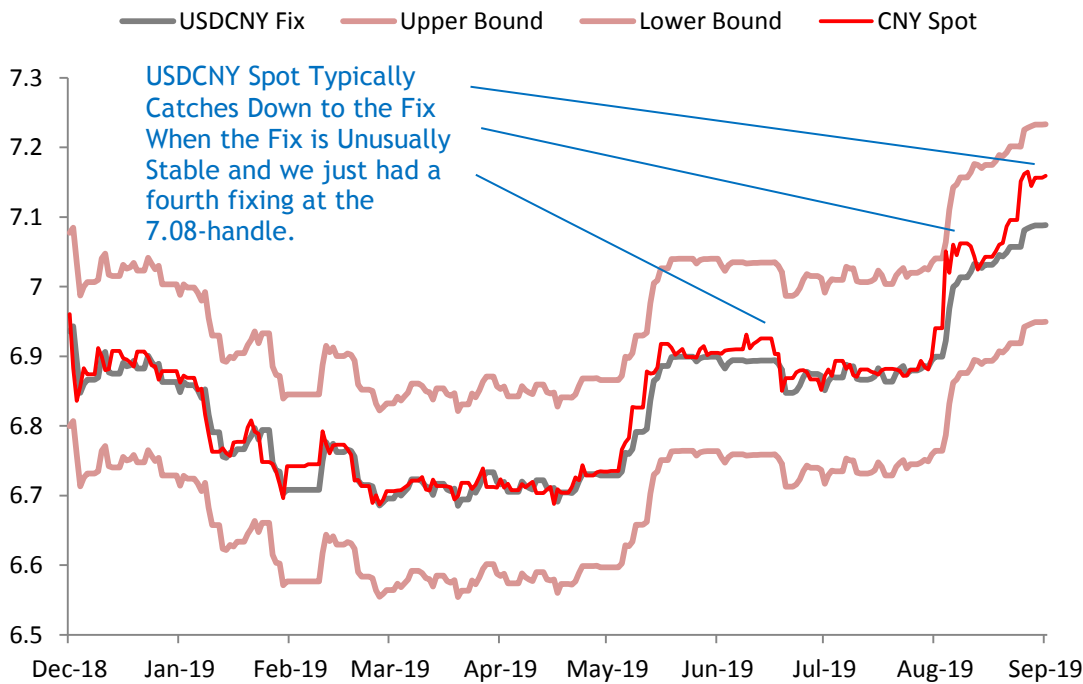
Sentiments are supported by expectations for the policymakers to provide “reasonably ample” liquidity and “reasonable growth” in aggregate financing as it implements a prudent monetary policy. The State Council also promised to increase counter-cyclical adjustments in economic policy. Equities rose at home in spite of the fact that new rounds of tariffs kicked in for US and China yesterday. We see lingering hopes of US-China trade tension de-escalation as USDJPY drifts higher and USD/North-Asians trade lower. USDCNH started today, rather elevated before retreating under the 7.17-figure ahead of the USDCNY fix. Spot had steadied within 7.16-7.18 for most of Asian hours, weighed by the stronger-than-expected fix as well as the above-50 Caixin PMI-mfg. We still think the USDCNY fixes provide a strong clue to where PBoC guides the RMB and possibly trade-talks development.

As such, we remain short-term bearish on the USDCNH and USDCNY even as a new round of tariffs kicked in from the US and China yesterday. As noted in our FX Daily [here](#) as well as our [FX Flash - RMB - The Fix Beckons The Spot](#), PBoC has been keeping the USDCNY reference rate around the 7.08-handle and today is the fifth consecutive session. This is done in a bid to suppress the CNY weakness against the USD and not likely to be sustainable in the long-term.

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USDCNY May Collapse Towards the Fix

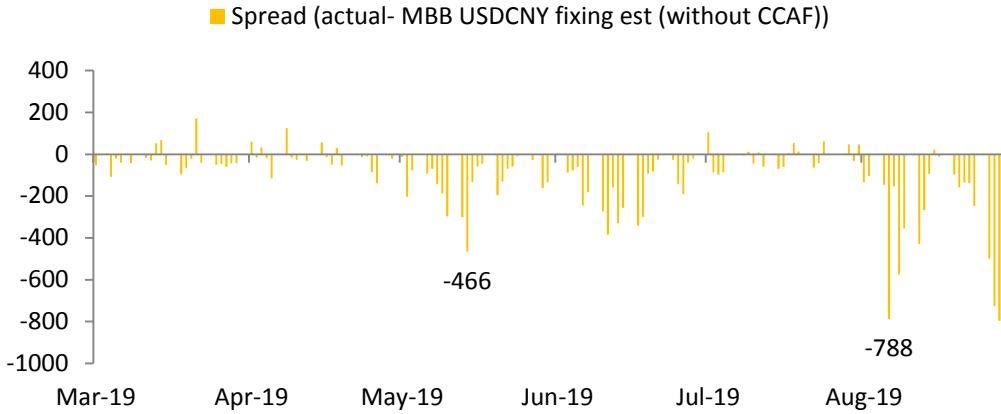


Source: Bloomberg, Maybank FX Research & Strategy

Signs That RMB Weakness is suppressed

- The CNY fix today is particularly strong (against the USD), out of the range of estimates polled by Bloomberg and stronger than ours. A more market-driven USDCNY fix would have been higher at 6.0998 (according to our final estimate).

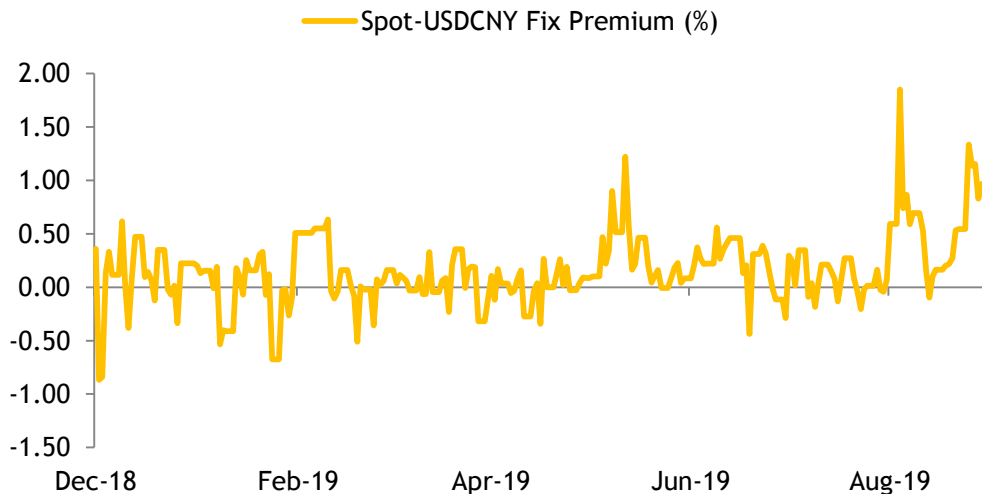
Actual USDCNY Fix Is Well Under Our Pure Model Estimate (without CCAF)



Note: CCAF denotes the Countercyclical Adjustment Factor, typically enhanced in times of market volatility.
 Source: Maybank FX Research & Strategy Estimates, Bloomberg

- The USDCNY reference rate is fixed at the 7.08-handle for the five consecutive sessions. That is becoming a more recognizable level and when a level becomes more recognizable like the 6.90 or the 7.00, there could be a lot more volatility when the levels like these are breached. We do not think PBoC desire spurts of volatility in the RMB.
- USDCNY spot now trades 1% above the fix - a result of a USDCNY fix that was too low. As mentioned before, wide deviations between the USDCNY spot and USDCNY fix do not last long.

USDCNY Spot-Fix Deviations Have Been Elevated, Cannot Last



Source: Bloomberg, Maybank FX Research & Strategy

Why is it unsustainable to Suppress RMB Weakness?

The current environment is one of broad USD strength with the DXY index just reached more than two-year high. By limiting the weakness in the CNY in this environment over a long period of time, CNY is at risk of losing its export competitiveness against other trading partners which could affect China's export performance. The CFETS RMB index has already risen from its low of 91.04-figure, last seen at 91.30.

One Has To Give... USDCNY Fix or the Spot

We see the recent USDCNY daily fixes as a show of confidence by PBoC that market forces will turn in their favour soon. That should come in the form of a USD collapse but the impetus for a USDCNY decline is stronger from a progression in the US-China trade talks. Our view for the 1st Sep tariffs to be delayed did not come true but we still think there could be potential positive developments and good progress in trade negotiations do not come fast and easy.

But What if Trade Tensions Remain Over the Longer Term

Despite our bearish bias in the near-term, we are aware of the possibility for the US-China tension to remain over the longer-term. Based on the newest round of tariffs imposed by the US on China (without taking into account substitution effect), there are a few critical levels for USDCNY that could be on the minds of investors should anyone be of the view that CNY would be allowed to cushion the impact of the US tariffs.

USDCNY Could Head Above 7.70

In light of the US tariffs of 15% on "\$300bn" of Chinese imports, USDCNY would have risen **above 7.70** in order to nullify the 15% impact on \$300bn of Chinese exports to the US as well as the 5% tariff hike on the \$250bn of Chinese exports to the US. That is taken off the price of USDCNY at around 6.90 before the latest phase of escalation triggered by Trump's announcement of the 10% tariffs on \$300bn of Chinese goods.

Or 7.40 Based on Past Performance in Trade War 2018

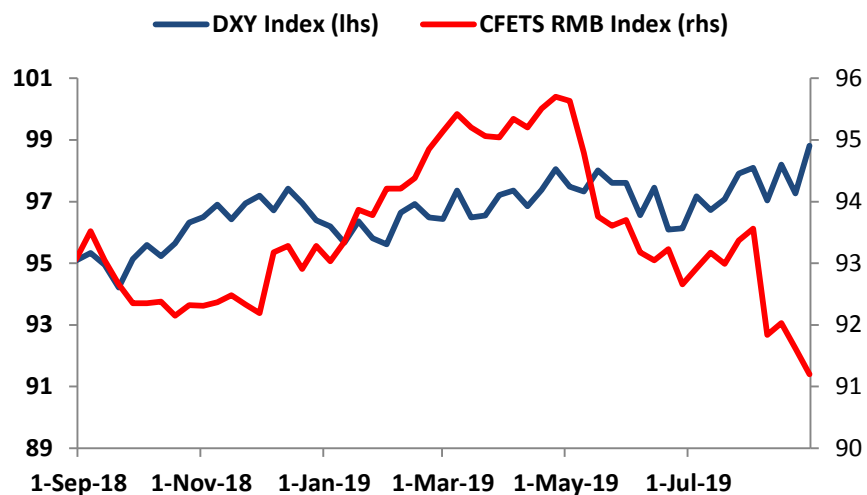
Another perspective to get a key level is that if we apply the 11% depreciation seen in the CNY against the USD last year that took USDCNY from 6.27 to 6.97 and apply it to the USDCNY from the start of the escalation this year, USDCNY could head above 7.40.

Regardless, all the key levels are still above the 7.1750, where the spot trades now (2 Sep). However, we do not think future moves in the CNY will be as explosive as the break of the 7 (unless USDCNY is fixed at 7.08-handle for a long period of time). Rather, PBoC has shown that it is more determined than before (compared to what was observed in 2018 trade war) to keep the RMB stable.

Upcoming Events to Watch in The Next Two Weeks

- 7th Sep - Foreign Reserves (Aug)
- 8th Sep - Trade data
- 9-15th Sep - Aggregate Finance, New Yuan Loans, Money Supply
- 10th Sep - CPI, PPI (Aug)

CNY TWI Deviates From the DXY as RMB Weakness Persists



Source: Bloomberg, Maybank FX Research & Strategy

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