

# RMB Watch

## Fending Off the Yuan bears

### Offshore Forward Points Rise

The 12M USDCNH forward points spiked from levels around 200 pips to north of 700 yesterday, before tapering off as we write. That triggered plenty of unwinding in the long USDCNH positions. The move came after two events (1) the announcement of the US-China trade talk that would happen on 22-23 Aug. China Vice Commerce Minister is said to visit the US for trade talks, at the invitation of the US. This would be the first trade talks since Jun. Wang Shouwen will lead a delegation to the US in late Aug. (2) Shanghai branch of PBoC announced that China has banned banks from certain lending activities. Commercial banks will no longer be able to use some interbank accounts to deposit or lend yuan offshore through free trade zone schemes. That would close some channels of outflows, tighten the offshore liquidity and as a result, effected the rise in the offshore forward points.

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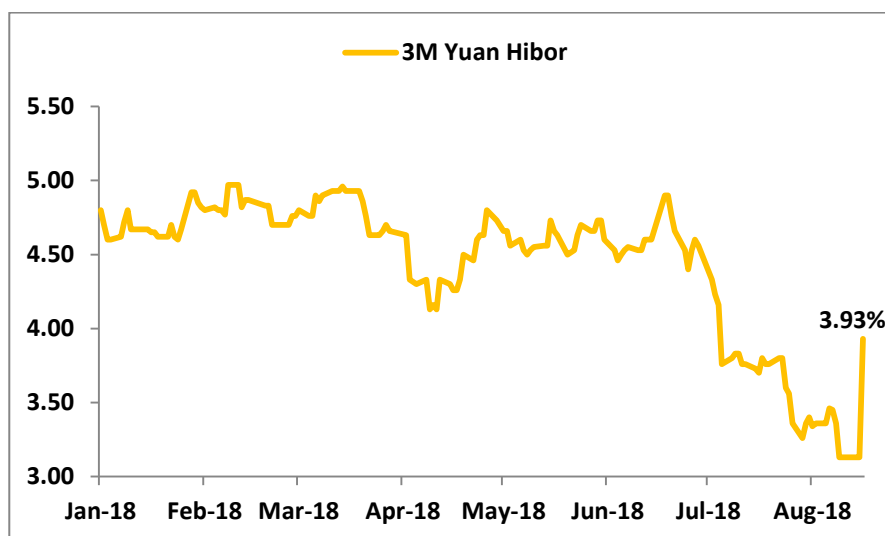
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**Chart 1: USDCNH Offshore Forward Points Surge**



Source: Bloomberg, Maybank FX Research & Strategy

### 3M Offshore Yuan Hibor Spikes Today



Source: Bloomberg, Maybank FX Research & Strategy

The 3-month yuan hibor spiked today, underscoring the tighter yuan liquidity conditions in the offshore market.

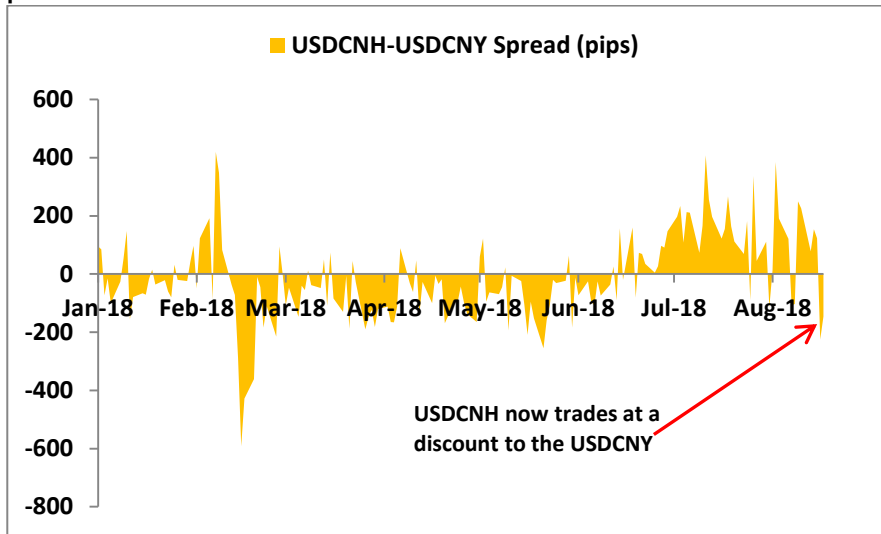
### China Gears Up for Longer-Term Support of RMB As Global Environment Remains Unfavourable

This was not the first measure to deter market players from speculating against the RMB. Earlier on 3 Aug, PBoC and SAFE reinstated the 20% reserve required for the forward sales of CNY. That was a time when USDCNY and USDCNH were testing the 6.90-figure as well. Clearly, the authorities were uncomfortable with the prices getting too close to the big 7-figure. This time, USDCNH were around 6.95 before falling sharply to a low of 6.85 this morning. We note that these are not one-off interventions like what we witnessed in past episodes of yuan weakness. These are policies and they are also walk-backs on their yuan internationalisation efforts. Their use of policy could be due to the fact that they do not want to burn their FX reserves in an environment of USD strength but it could also suggest that they are gearing up for a longer-term battle against yuan bears in case the trade war with the US drag on and as the external environment remains unfavourable for EM currencies in general including RMB.

### The Latest Measure on Offshore Lending Coincides With the US-China Trade Talks

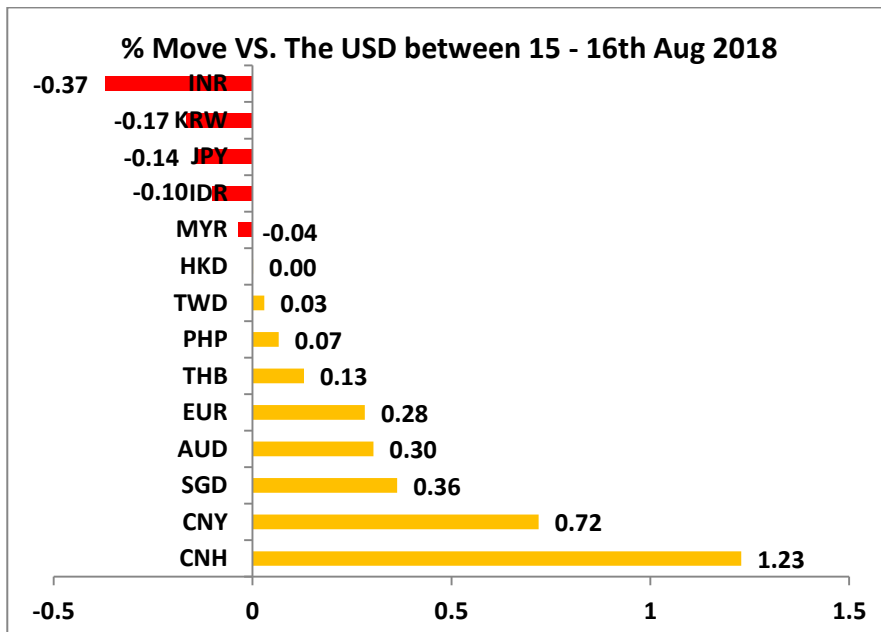
The latest measure of shutting down the channel for banks to deposit or lend offshore yuan via the free trade zones is also nicely timed right after the announcement of the US-China trade talks that is scheduled on 22-23 Aug. That added to the feel-good factor to the RMB. USDCNH slips under the USDCNY as a result.

**USDCNH Now Trades At a Discount to USDCNY after months of persistent Premium**



Source: Bloomberg, Maybank FX Research & Strategy

However, the broad weakness in the USD was reversed out after Asian hours when Trump made fresh threats to impose more sanctions should Turkey fail to release the US pastor, Andrew Brunson.



Source: Bloomberg, Maybank FX Research & Strategy

Nonetheless, the moves in the currencies against the USD suggest that market players were cautiously optimistic of the trade talks. We still hold the view that trade war premium is significant at this point. We remain optimistic that the trade war premium could ease should the US become more focus on mid-term elections at home. In fact, President Xi seems to be facing increasing pressure at home to handle the trade war especially after a Chinese pharmaceutical company supplied 250,000 substandard vaccine doses to children. Some parents held a protest, blaming the government for its lack of oversight. This scandal, in a backdrop of a slowing economy, adds pressure on Xi to ensure that the trade war does not have further lasting impact on China’s growth or risk facing further social grievances.

While we retain some optimism on the trade war front, there are increasing risks for Asian FX emerging elsewhere. We refer to the 1) standoff between Erdogan and Trump that has triggered more Asian FX selling; 2) the potential for EURUSD to head lower in the next 2-3 months given the uncertainty on Italy's budget plans (Sep) and German Bavarian State election (in Oct) amid a negative carry environment. A EUR pullback could lift USDAsians and increase the upside risks to our USDCNY and USDCNH for the rest of the year.

The external environment has certainly increased our caution on the RMB vs. the USD and validates the recent FX measures undertaken by China. To further reinforce the message that China prefers a more stable RMB, the USDCNY reference rate is fixed well under most projections including our own in the past few sessions. As such, while we think market forces could still drive the USDCNH higher but in the face of PBoC, yuan bears may be much weaker than before.

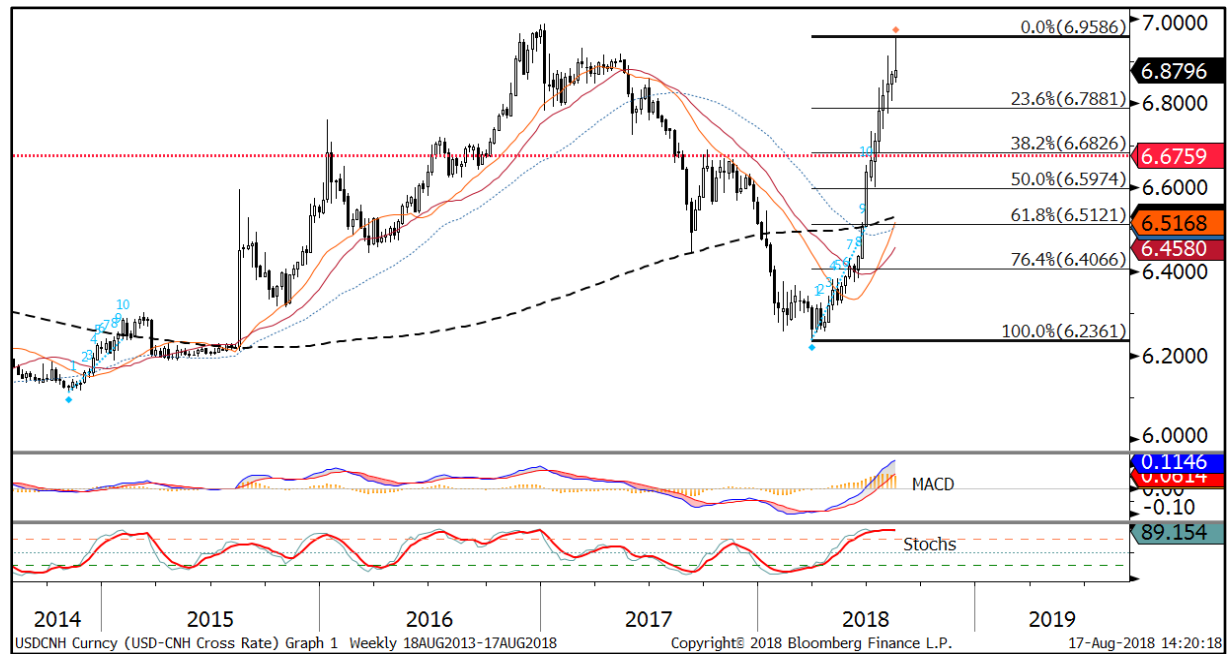
## RMB On The Technical Charts

(USDCNH daily) - Risks Turning Lower



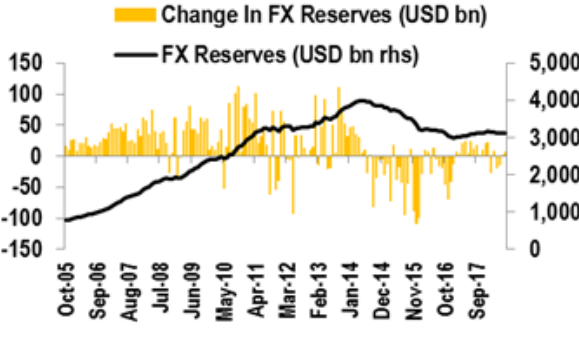

We had pointed out that the USDCNH looks a tad toppish in the last issue of the RMB Watch. However, USDCNH went on to a high of 6.9586 before coming off sharply. We still hold our view that the USDCNH may not head a lot higher from here. This pair requires a break of the 21-dma (6.8429) to head lower. The candlestick this week is poised to end as a gravestone doji. If the resistance at 6.9586 holds, there could be a double top.

(USDCNH Weekly) - Gravestone Doji

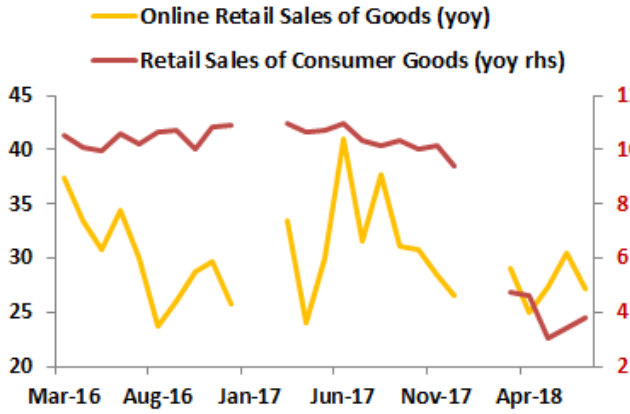
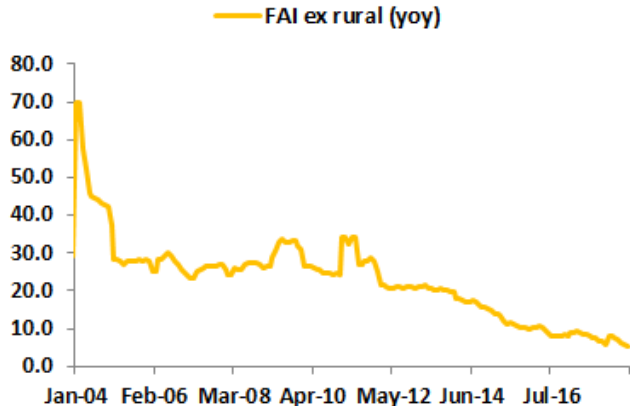


Source: Bloomberg, Maybank FX Research & Strategy

## Keeping Track

Date	Events/Data Headlines	More Details, Impact and Views	Relevant Charts (if any)
3 Aug	<p><b><u>Clamping Down on FX Speculators</u></b></p> <p>PBoC and SAFE reinstated the 20% reserve required for the forward sales of CNY.</p>	<p>USDCNH came off sharply from the 6.90-handle to levels under 6.85. The reserve requirement was removed last Sep and first introduced on 2<sup>nd</sup> Sept 2015.</p>	
7 Aug	<p><b><u>Foreign Reserves Rise in Jul</u></b></p> <p>Foreign reserves posted a surprise rise to U\$3.118trn vs. the previous U\$3.107trn.</p>	<p>Consensus expected a drop in forex reserves given the immense pressure that the yuan faces. However this latest print suggests that forex reserves have not been utilized to defend the RMB. This underscores the fact that spot prices are largely market driven in reaction to downside pressure on domestic demand, easing measures and trade war fears.</p>	
8 Aug	<p><b><u>Trade Surplus Narrows Though Growth Beat Expectations</u></b></p>	<p>Exports and imports growth beat expectations this month but full effect of the trade war is likely not seen yet. Strong imports growth indicates stronger domestic demand but that could also be a ramp-up of purchases as more tariffs are being considered.</p>	

\*News Sources from Xinhua, Bloomberg, China Daily, China Securities Journal, China Business News; Data from CEIC, Bloomberg, NBS, SAFE, PBoC

Date	Events/Data Headlines	More Details, Impact and Views	Relevant Charts (if any)
14 Aug	<p><b><u>Softer Activity Data for July</u></b></p> <p>Activity Data came in under consensus for Jul. Retail sales slowed to 8.8%y/y from previous 9.0%. IP steadied around 6.0% and FAI (urban) decelerated to 5.5%y/y from previous 6.6%</p>	<p>NBS stressed that the drop in the fixed asset investment growth was due to high base and that the “steady economic operation” in July was “not easy”, also warned of effects of trade tension showing up on global economy.</p> <p><i>NBS' comments seem to suggest that the government is doing all it can to support growth and also to allude the domestic slowdown to trade war. Regardless, bets on a near-term RRR cut likely to rise in Oct. We still hold the view that trade tensions should ease in time when the US are more focused on the mid-term elections back home and when it is over.</i></p>	
14 Aug	<p><b><u>Boosting Domestic Demand</u></b></p> <p>The Ministry of Finance instructed local governments to quicken their issuance and use of special bonds for investment.</p>	<p>This move is reportedly meant to ensure a better use of these special bonds to “stabilize investment, expand domestic demand and improvement weak links”. According to the official document, provincial level regions should make scientific plans for the bond issuance in Aug and Sep in order to accelerate bond issuance. By end Sep, new special bonds issued in the first nine months should account for no less than 80% of the CNY1.35trn quota this year. The remainder should be issued mainly in Oct.</p> <p><i>This is an assurance that the government is increasing pressure on the local government to boost investment and domestic demand after the shocking drop in FAI (rural)</i></p>	

\*News Sources from Xinhua, Bloomberg, China Daily, China Securities Journal, China Business News; Data from CEIC, Bloomberg, NBS, SAFE, PBoC

### **Upcoming Events to Watch**

20 - 23 Aug - Planned Hearings on US Trade Tariff on U\$200bn of China Goods (10% tariff could be revised higher to 25%)

22 - 23 Aug - US-China Trade Talks in Washington

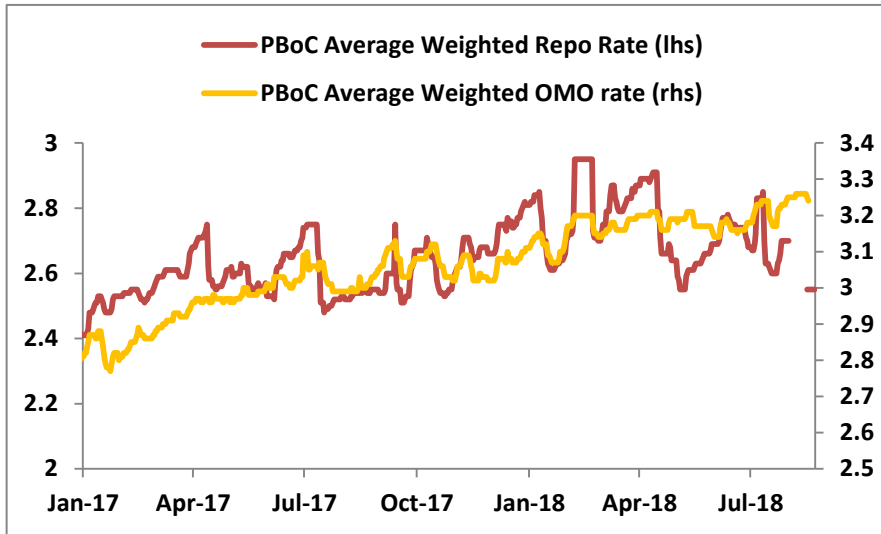
24 - 25 Aug - Jackson Hole Symposium

27 Aug - Industrial Profits



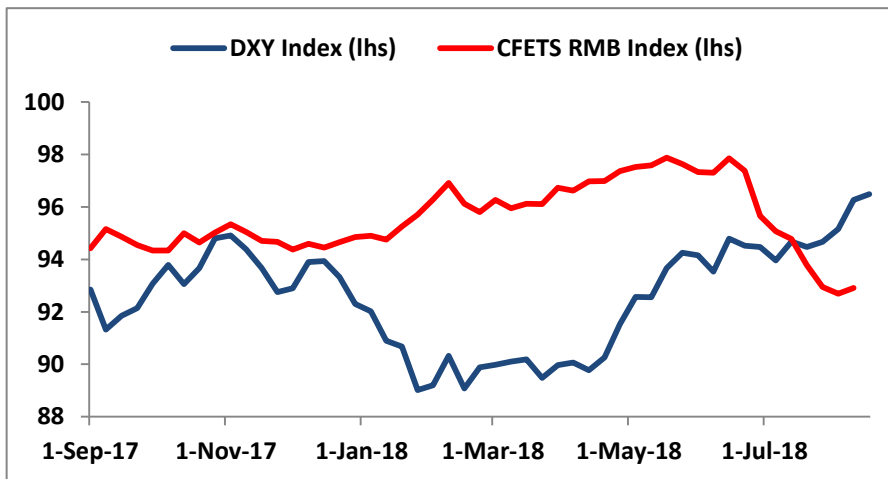
## Charts We Monitor

Chart 1: Repo Rates Dropped while OMO still remain rather Supported



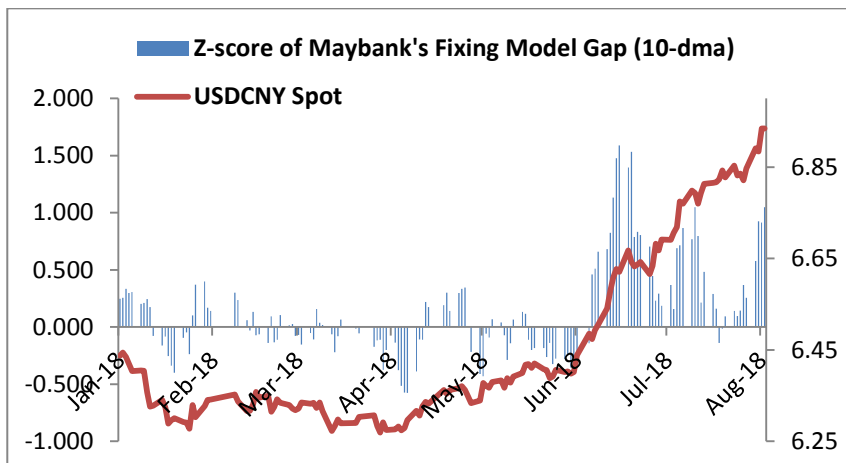
Source: Bloomberg Calculation, Maybank FX Research & Strategy

Chart 2: CFETS RMB Index Seems To Have Bottomed



Source: Bloomberg, Maybank FX Research & Strategy

Chart 3: Deviations between actual USDCNY fixing and our model projections Widens



Source: Maybank FX Research & Strategy Estimates, Bloomberg

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