Jun 14, 2021

Maybank

FX

Global

RMB Watch

FOMC Plays and Other Bearish Risks

Interim Weakness

Key Points:

- Positioning ahead of the FOMC meeting and thinner liquidity in the absence of onshore markets in mainland China and Hong Kong saw USDCNH rise above the 6.41-figure today. The RMB was not helped the least by reminders from senior officials at the Lujiazui Forum (last week) that there are more avenues for outflows such as an expansion of the Qualified Domestic Limited Partnership Program (that enables global asset managers to sell foreign investment products to local institutional investors and high net worth individuals). The FOMC policy decision is still a key event and should the Fed maintain its dovish messaging, we continue to look for USDCNH and USDCNY to revert to a gradual decline.

- G7 leaders displayed a somewhat united front, calling for a new phase of WHO investigations into the origins of COVID-19 in China. The group also urged China to respect human rights and freedom in Xinjiang and Hong Kong. Another key development out of the meeting at Cornwall, UK was the infrastructure plan that could be an alternative to China's Belt Road Initiative. The White House said the "Build Back Better World" (B3W) initiative aims to provide a transparent infrastructure partnership to help narrow the $40trn needed in the developing countries, a sign of greater frictions between G7 and China in the future.

- **Technical Analysis:** USDCNH has upside risks towards 6.44 but we eye FOMC meeting that could reverse gains. EURCNH was last at 7.7680, retaining bearish bias. MYRCNH and SGDCNH can remain on the climb towards 1.5640 and 4.85 respectively.

What We Watch (14 - 28 Jun):

Date	Data	Month
14 - 16 Jun	1Y MLF	n.a
16 Jun	Retail sales, Industrial Production, Fixed Assets Ex Rural	May
17 Jun	FOMC Policy Decision	
17 Jun	SWIFT Global Payments	May
17 Jun	New Home Prices	May
18 Jun	FX Net Settlements	May
21 Jun	1Y, 5Y Loan Prime Rate	Jun
25 Jun	BoP Current Account Balance	1Q Final
27 Jun	Industrial Profits	May

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Where Has RMB Been?
USDCNH has retraced higher since its year low of 6.3525 recorded on 31 May. Price action was mostly consolidative within 6.35-6.40 range before a break-out today in the absence of onshore markets in mainland China and Hong Kong. CNH weakness is exacerbated by thin liquidity, FOMC policy decision this week and some anticipations of outflows as local firms make dividend payments for shares listed in Hong Kong.

Pressure on the RMB

Ahead of the Dragon Boat Festival break (12-14 Jun) that has onshore markets in China closed today (14 Jun), the Lujiazui Forum was held 10-11 Jun and a number of senior officials spoke including PBoC Yi Gang, SAFE Chief Pan Gongsheng, former PBoC Governor Zhou Xiaochuan amongst others. We heard

(1) a clear warning from CBRIC Guo Shuqing on retail speculators of property, RMB, commodities that they will "pay a heavy price".

(2) PBoC Governor Yi Gang's stress on **slower growth**, **mild inflation** (under 2% expected) and **mid-level interest rates** (sandwiched between lower levels in major developed countries and higher levels seen in developing and emerging economies) could be another attempt to **discourage one-way bets on RMB appreciation**.

(3) SAFE Chief Pan Gongsheng (another Deputy Governor of PBoC) flagged **capital account liberalization moves** – expansions of the Qualified Domestic Limited Partnership (QDLP) and a Qualified Foreign Limited Partnership trial in Lingang New Area– of Shanghai's free-trade-zone. The FTZ was expanded to include Lingang New Area in 2019 so as to promote greater trade, investment, finance, talents and information mobility. Along with the upcoming Southbound bond connect (that could enable Chinese investors to buy HKD and USD-denominated bonds), **officials seem keen to promote the upcoming avenues for outflows that could weigh on the RMB in the medium term.**

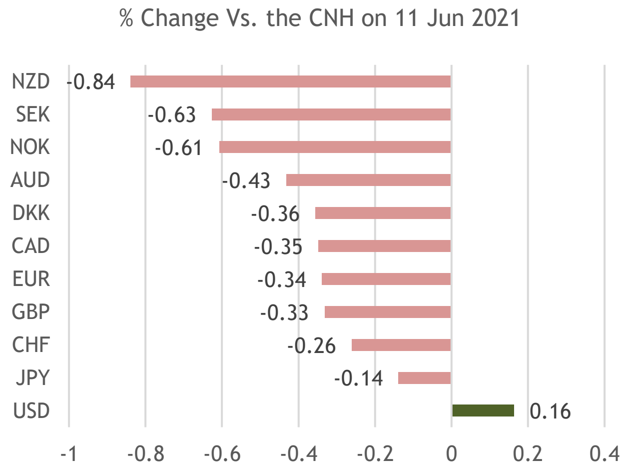
Taken together, China is clearly taking advantage of the current benign and low volatility environment to liberalize China's capital account. This is a much better timing (for RMB) compared to its liberalization efforts in 2013-15 period ahead of the IMF SDR inclusion when China juggled yuan internationalization efforts with slower growth, concerns on hot money outflow and falling FX reserves.

We concur that RMB would see a slower rate of appreciation for the rest of the year (relative to 2020). This remains in line with our view for USDCNY to head towards 6.25 in the next 6 months, notwithstanding some upside pressure in the near-term as FOMC meeting comes into focus.

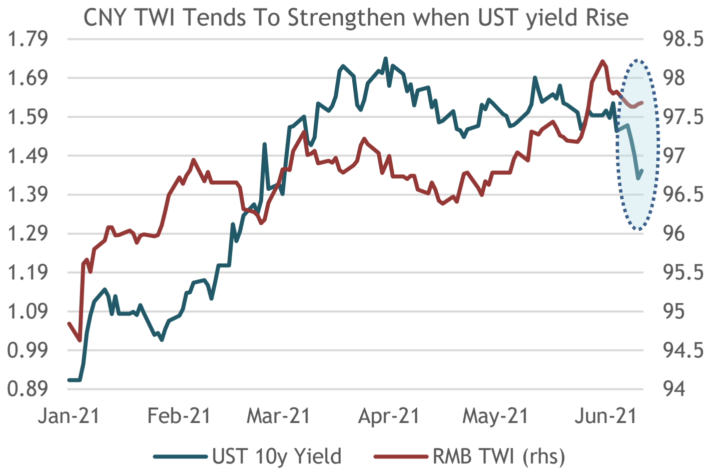
We saw a jump in the UST yields and USD last Fri as market players cautiously position for the FOMC policy meeting this week. USDCNH too was brought above the 6.40-figure by Mon (14 Jun) and we may possibly see further USD strength ahead of the event. However, it is also interesting to note that even as USDCNY and USDCNH were brought higher last Fri, momentum was tepid relative to peers resulting in trade-weighted gains for the RMB.

This was evident in the left chart where most other (lower yielding) DM currencies posted declines against CNH last Fri. The CFETS-weighted TWI of the RMB on the right chart also rose a tad alongside the small rise in 10y UST yield. In fact, since the start of the year, the rise in the UST yields coincided with the periods of appreciation in the CNY TWI. Investors had showed preference for the RMB when US treasuries were under heavy selling pressure.

CNH Weakened Against USD, But Stayed Resilient Amongst Other Peers



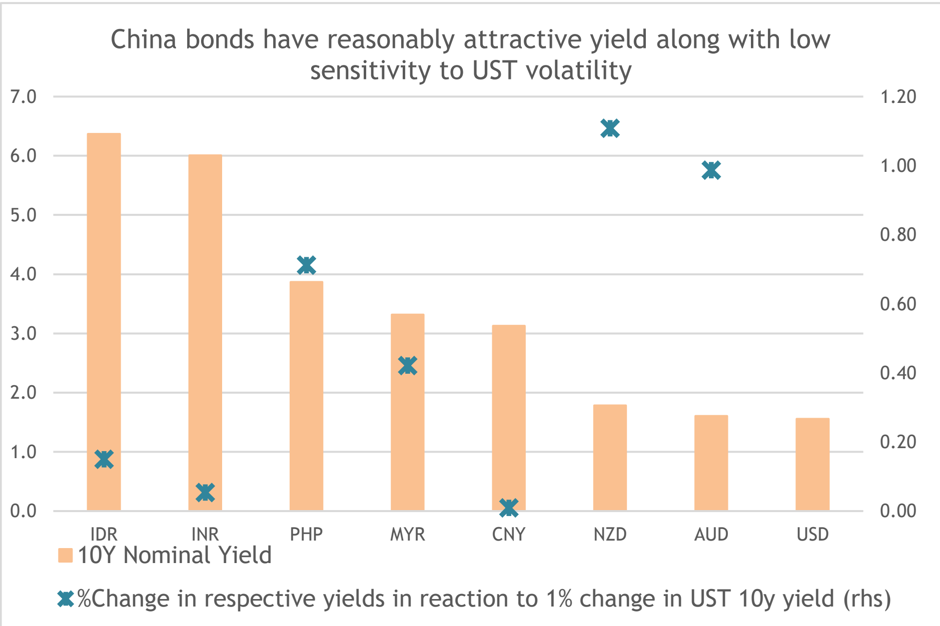
RMB tends to strengthen against Peers When UST Yields Rise



Source: Bloomberg, Maybank FX Research & Strategy

Based on the chart below, 10y China Government Bond displayed lower sensitivity to US treasury yield moves compared to peers since the start of the year. At the same time, the bonds retain a fairly superior level of yield compared to peers. Along with effective pandemic containment and strong macro fundamentals, China bonds remain relatively attractive to investors resulting in the outperformance of the RMB.

China Government Bonds Remain Attractive given its relatively higher yield and low sensitivity to US Treasuries.



Source: Maybank FX Research & Strategy, Bloomberg
Note: Nominal yields are as of 8 Jun and data for 1 Jan-8 Jun are used to compute sensitivity

View on FOMC is Key in the Near-term

At this point, it may be relevant to note that positioning ahead of the FOMC could very well be reversed should the upgrade in economic outlook expected at the meeting be accompanied with the consistent Fed's messaging that inflationary pressures are transitory (and will abate) and that the Fed is likely to continue to stay behind the curve for now. Bear in mind that the Fed is operating under an Average Inflation Targeting (AIT) regime and that they will be tolerant of inflation overshoots. As such, the FoMC decision on Thu (Asia morning) may well shape up to be a non-event, if markets are mostly convinced of Fed keeping policy stance status quo. And this implies that we may well get that risk-on, goldilocks environment for carry and pro-cyclical FX to strengthen.

Beyond the near-term event-risk and notwithstanding capital account liberalization measures that enable domestic investors to buy foreign assets, we still expect enduring foreign demand for Chinese assets (bonds and equities), along with substantial current account surplus and broader USD weakness to bring about an eventual reversion of the USDCNY towards 6.25.

Update on G7 and China

The G7 leaders (Canada, France, Germany, Italy, Japan, UK and US) displayed a somewhat united front, calling for a new phase of WHO investigations into the origins of COVID-19 in China, backing Australia's call since 2020. The communique also urged China to respect human rights and freedom in Xinjiang and Hong Kong. On the other hand, condemnation on China's trade measures against Australia was weaker than expected as the group "seeks to consult on collective approaches to challenging non-market policies and practices which undermine the fair and transparent operation of the global economy". Another key development out of the meeting at Cornwall, UK was the infrastructure plan that could be an alternative to China's Belt Road Initiative. The White House said the "Build Back Better World" (B3W) initiative aims to provide a transparent infrastructure partnership to help narrow the $40trn needed by developing countries.

A spokesperson of Chinese Embassy in the UK remarked that the criticisms were based on "distorted facts" and urged the group to "stop meddling in China's internal affairs". In response to accusations of "non-market policies", the embassy highlighted that China's total tariff level was lowered to 7.5% since Nov 2018 and the country remains committed to opening up and creating an environment where domestic and foreign enterprises can compete on a levelled playing field. Ahead of the G7 meeting, China NPCSC approved the "anti-foreign sanctions law" on 10 Jun and will set up a task force to enforce this new anti-sanction law. Under this new law, foreign and chinese individuals and companies involved in sanctions against China will be taken to court and forced to "stop the infringement and to pay compensation losses". This came after the US Senate passed a industrial policy bill that enables the White House to impose sanctions on Chinese officials for cyberattacks, human rights violations and IP theft.

These signal greater conflict ahead between the Western world and China but a lack of concrete actions at this point also translates to minimal impact on the RMB for now.

USDCNH (Daily)- Bullish RIsks

USDCNH hovered around 6.4150, breaking above the 6.4080 resistance (23.6% Fibonacci retracement of the Mar-May drop).

Momentum indicators are bullish and the clearance of the 6.4080-resistance could open the way towards 6.4420.

Support at 6.35.

EURCNH (Daily) - Bearish Momentum Intact

EURCNH slipped to recent lows before rebounding. Cross was last seen around 7.7600.

Momentum indicators remain bearish and we cannot rule out a test of the nearby support at 7.7340. A break there opens the way towards the next at 7.6900.

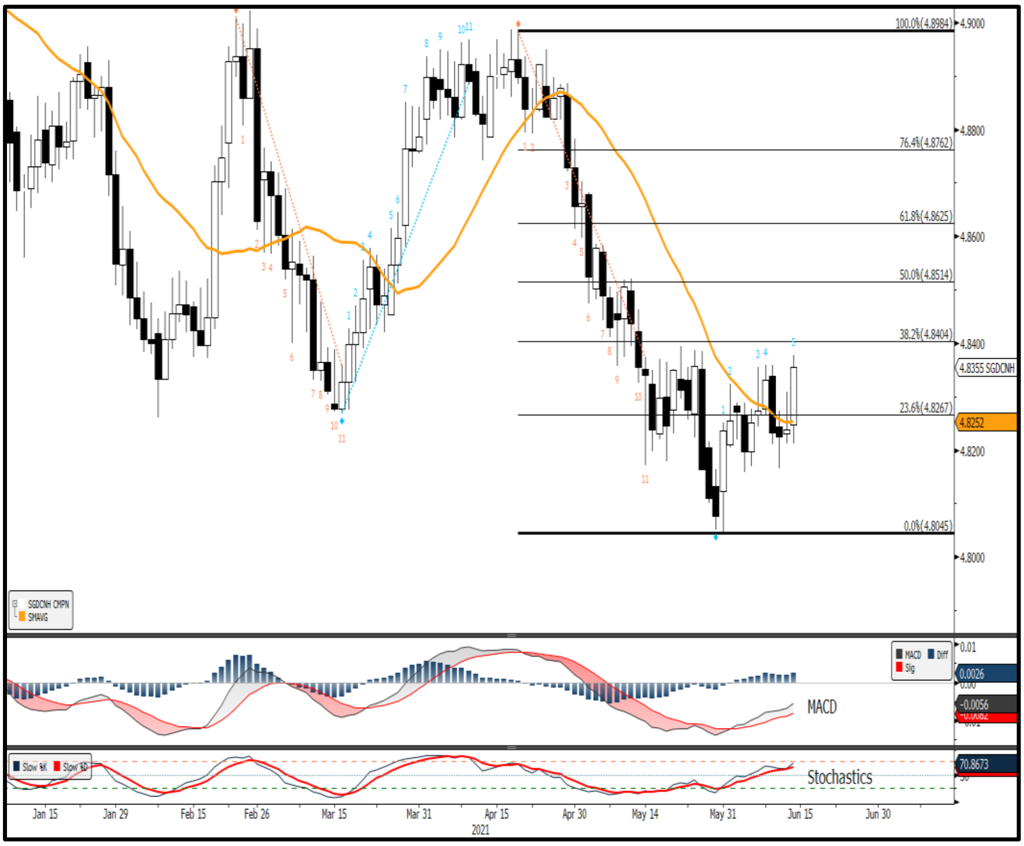
Resistance at 7.7820. We see two-way trades in the near-term with risks skew on net slightly to the downside.

MYRCNH (daily) – Risks to the Upside

Our bullish view on the MYRCNH played out for the past two weeks and this cross was last around 1.5590 and our view for the cross to head towards the 1.5637 resistance is almost coming to fruition. Momentum remains bullish

Support is seen around 1.5568 (resistance turned support) before the next at 1.5480.

SGDCNH (Daily) – Slow Grind Higher



SGDCNH was on a slower grind higher relative to the MYRCNH and was last around 4.8356, yet to hit our first target at 4.84.

Nonetheless, momentum remains bullish and the SGDCNH can continue to climb towards 4.8404 before the next at 4.8514 (50% Fibonacci retracement of the Apr-May fall).

Support at 4.8252 (21-dma, marked by yellow line) before the next at 4.8045.

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