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Article

Ripping up the rule book on currencies and trade

In March, G20 members promised to avoid competitive devaluations for trade gains. The overnight move to fix the Chinese yuan lower suggests that may have been a hollow pledge. But is this really an active devaluation?

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USD: Amid global trade wars, currencies could become trade tools

Looking at the 0.5% higher fixing in USD/CNY overnight and the move to 6.73 in USD/CNH one could be forgiven for thinking that China is threatening a devaluation in retaliation to rising US tariffs (next set implemented this Friday). However, the move looks passive so far i.e. investors positioning for a weaker CNY on the back of slower trade growth rather than this being an active devaluation by the People's Bank of China. Equally, the one-year USDCNH forward points are very subdued at +650pts versus the +2500pts levels seen in 2015/16. However, these moves do beg the question whether any nation should respect the G20 Communique, most recently outlined in March this year, that members would avoid competitive devaluations for trade gains. Probably at this stage the nation most likely to flout those agreements is the US, thus presenting a left-field risk to US dollar bulls. For the near term, however, there is no sign in the polls or US domestic data that Trump's aggressive trade policies are having any ill-effects. And with emerging markets clearly under pressure – including good quality positions in Poland – the dollar will likely win out in the near term. DXY to stay bid in a 94.50-95.50 ahead of good US jobs data later this week.

EUR: A slight easing in German political risk

The euro is enjoying a modest lift from news that the German CDU & CSU coalition members appeared to have reached an agreement on migration policy. Yet the US-eurozone macro and rate divergence story looks set to stay in place this week – which should be keeping a lid on the EUR/USD rally. 1.1690/1.1720 resistance is expected to hold.

GBP: Brexit fudge

We're still wary that EUR/GBP is on the verge of an upside breakout given its exit from a period of very low volatility. Prime Minister Theresa May looks set to face down the Brexiteers later this week, but may be no closer to a Brexit deal with the EU. 0.8900 remains the risk. The Czech koruna and Polish zloty remain vulnerable on positioning.

SEK: Temporary respite for the SEK?

The Riksbank meet to set policy today and an [unchanged communication strategy](#) could see a reiteration of a first hike in December. That could be backed up by some modest upward revisions to growth and inflation forecasts since the Swedish krona (SEK) is around 4% weaker than the Riksbank expected it to be in 3Q18. Yet the unravelling of the global trading system is a clear negative to the SEK as are headwinds from the Swedish housing sector and domestic politics. Any rally in the SEK to the EUR/10.35 area looks unlikely to be sustained and we have EUR/SEK targets well above 10.50 for later in the year.

Chris Turner

Global Head of Strategy and Head of EMEA and LATAM Research

+44 20 7767 1610

chris.turner@ing.com

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