

Article | 8 October 2018

FX

## Global FX: Turning into a bloodbath

Chinese equity markets and the yuan play catch-up to last week's turmoil in global markets – with both sliding lower despite another 100 basis point RRR cut



Source: Shutterstock

### ➔ USD: Chinese markets play catch-up to last week's global turmoil

The return of Chinese financial markets after the Golden Week holiday is setting the tone for the rest of the world in a week that begins with the US, Canada and Japan all out on holiday today. To a large degree, both Chinese equity markets and the Chinese yuan are playing catch-up to last week's turmoil in global markets – with both sliding lower despite the People's Bank of China returning with another targeted cut in the reserve requirement ratio (by 100 basis points). The PBoC also fixed USD/CNY just shy of the 6.90 level (the reference rate today was 6.8957) – which was broadly in line with our expectations given the yield-driven moves seen in the dollar last week. Yet, the spillover effects to other CNY-sensitive currencies has been fairly limited; we usually view the Australian dollar as a litmus test here and the currency is trading fairly neutral this morning. This corroborates our view of a 'catch-up' theme in Chinese markets – and we think the PBoC not opting to fix USD/CNY anything north of 6.90 might have provided some minor relief – amid a myriad of woes – to risky assets. Our [G10 FX Week Ahead](#) notes that the stock market rout may keep high-beta FX under pressure.

### ➔ **EUR: Moment of truth for the Italian budget & German macro data**

While the Italian budget noise continues to be unhelpful for the euro – our base case is for 10-year BTP/Bund spreads to broadly hold in the upper half of the 200-300bp range over the coming months. This takes into account a likely one-notch downgrade from Moody's. If S&P also downgrades Italy's credit rating –and not just the outlook as our base case assumes – a sustained break above 300 basis points might unfold. In the absence of this, expect EUR/USD to trade fairly neutral around the 1.15 level with German data and the ECB minutes to note this week.

### ➔ **JPY: Tentatively calling a top in USD/JPY as bond rout turns to stock rout**

While rising US bond yields had taken USD/JPY up to an intraday high of 1.1455 earlier last week, the upward trend channel has stalled – with the pair moving back below 114. Part of the reason is the broad sell-off in global tech stocks – in particular the Nasdaq – which may well have fuelled yen repatriation flows. We are tentatively inclined to say that this may be a short-term top for USD/JPY – but will need to see a sustained move below 1.1330/50 to provide confirmation of this. External risks ahead include ongoing US stock market woes, any further negative US-China trade war rhetoric, negative global growth sentiment from the IMF World Economic Outlook report (Tuesday). It doesn't look pretty – and the yen should win here.

### ⬆️ **BRL: Bolsonaro win could see move to 3.70 but a lot of good news priced in**

After the first round of Brazil's Presidential elections, [ING's Gustavo Rangel notes](#) that the results diverged materially from the current polls – with a strong anti-establishment wave helping unseat many traditional forces. In the presidential race, right-leaning candidate Jair Bolsonaro led left-leaning runner-up Fernando Haddad by 17pts. Bolsonaro's strong momentum gives him an edge, but a more moderate Haddad also bodes well for local assets. We continue to expect the Brazilian real (BRL) to trade with a constructive (but yet volatile) bias, with some risk of USD/BRL temporarily dropping below our year-end forecast of 3.70. But given the sharp rally that has already occurred, the room for additional BRL appreciation seems more limited. The second round of voting takes place on 28 October and we note a final election call remains difficult – expect some policy moderation from both candidates.

## Author

### Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

[viraj.patel@ing.com](mailto:viraj.patel@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit [www.ing.com](http://www.ing.com).