

## USD/CNY slips its anchor, global FX follows

While most suspect President Trump's China tweets come from his 'Art of the Deal' handbook, FX markets are worried that there could be more to it. USD/CNY has slipped its anchor near 6.70 and is dragging activity currencies with it. We take a quick look at which currencies are most at risk if this week's tension aren't merely a small bump in the road to a deal



Source: Shutterstock

### USD/CNY breaks free

[We hold a baseline view that Chinese authorities will want to keep USD/CNY fairly stable this year.](#)

This is premised on a trade deal being concluded over perhaps some time in 3Q19. We had also felt that the stability in USD/CNY between February and April had been an important factor contributing to [declining cross-asset market volatility](#) and the supportive risk environment.

This week's move in USD/CNY has, therefore, come as a surprise and jolted markets out of their comfort zone. Recall USD/CNY can trade +/- 2% around the People's Bank of China daily fixing – making the fixing a very important tool in influencing currency markets. We're also focusing on

how much weaker the offshore CNH is priced than the onshore – over the last year the ‘basis’ between USD/CNH and USD/CNY has gone as wide as 400 pips.

[Read why we think a sharp yuan appreciation or depreciation is unlikely in 2019](#)

## USD/CNY starts to push higher again



Source: Bloomberg, ING

## What if this trade spat is a little more serious?

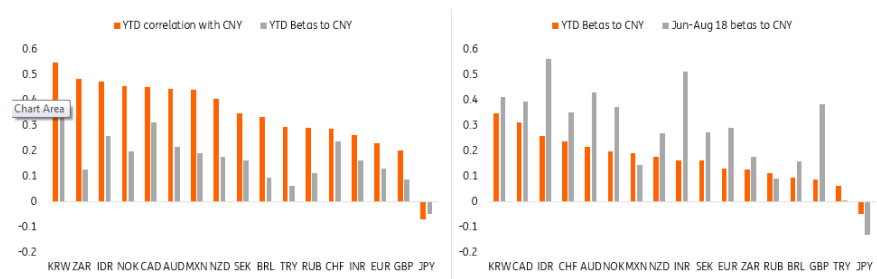
We all assume that something will happen before Friday morning's deadline to raise US tariffs on USD 200bn worth of Chinese goods to 25% from 10%. By the looks of it, financial markets are a little more concerned that the ‘reneging’ allegations against China from President Trump's trade team are a little more serious than last-minute fine-tuning.

Albeit seemingly small, there is still a chance that US-China trade relations are not back on track by Friday morning. The imposition of higher US tariffs (even for the short term) would un-nerve global FX markets. Even if the PBOC were to continue fixing USD/CNY near today's 6.76 fixing level, the onshore could press the 2% daily limit near 6.90 and USD/CNH could trade 6.94. USD/CNY retesting the 7.00 level was certainly not in the 2019 investment script.

Given trade linkages, we would expect emerging market and pro-activity currencies in the G10 space to come under pressure. Checking year-to-date correlations with the CNY (we look at daily changes versus the USD), the familiar suspects of the KRW, ZAR, IDR, CAD and NOK would look most vulnerable to more surprise weakness. And looking at betas both for this year and during last year's CNY sell-off, a similar mix of currencies is seen as well.

Clearly, the lack of correlation with the CNY is a distinct advantage for the JPY right now, but also for the dollar, which should stay bid if emerging FX were to come under increasing pressure.

## Correlations and betas with CNY (calculated via daily changes against the dollar)



Source: Bloomberg, ING

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