

Correlations with China's yuan are weakening in Asia

The Chinese yuan still exhibits a strong gravitational pull on other Asian currencies, but it is not as strong this year as it has been



Source: Shutterstock

Gravity model of FX

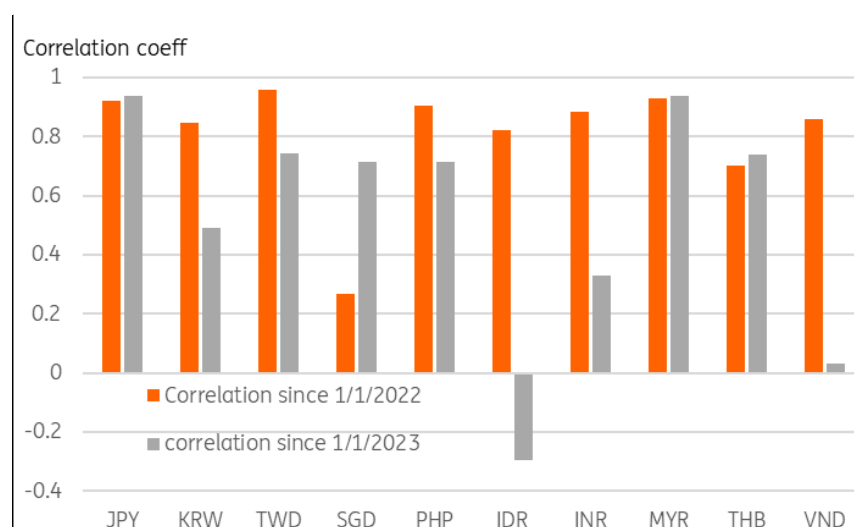
There is such a thing as the "gravity model of foreign trade", and if you are interested, [the following Wiki link](#) will tell you as much as you probably want to know.

As far as I am aware, there is no such thing as the "gravity model of FX", though I find it is a useful analogy for thinking about currencies in the Asia-Pacific region. Maybe I can try to popularise it...

If you use the analogy of the solar system to think about currencies, then the US dollar is clearly the sun, around which all other currencies revolve. But there are patches of space where other large celestial bodies, further away from the sun can have a significant influence, and here in the APAC region, the CNY is clearly that currency. Think of it as the gas-giant Jupiter if you want.

Much of the time, it is the ebb and flow of the USD that drives exchange rates in the region, and cross rates remain fairly steady. That isn't happening now, and the reason for this lies in the CNY.

Asian FX correlations with the CNY



Source: CEIC, ING

One of these currencies is doing its own thing

Right now, China is bucking the global trend and cutting, not raising rates, reflecting what is a very mediocre and rather disappointing reopening following zero-Covid. We have written about this in a couple of notes recently which you can access [here](#), and [here](#). And one of the upshots of this is that the CNY has been weakening, with the People's Bank of China (PBoC) seemingly quite tolerant of such weakness with all policy levers being considered to help offset the economy's weakness.

Furthermore, what we see is that the gravitational pull - as described by the correlation coefficient - of the CNY is dragging down some local currencies with it, though the strength of this pull is weaker than in the past. This tends to confirm that what is happening to the CNY right now is more than just a generalised bout of USD strength taking all currencies along for the ride, but something more unique to China.

Two currencies do remain tightly bound to the Chinese yuan, namely the Japanese yen and the Malaysian Ringgit. Both are historically at the higher end of correlations, reflecting strong trade links and perhaps as a result, these two currencies remain in a tight orbit to the CNY.

Elsewhere, the links are very much weaker, or in the case of the Indonesian rupiah, actually negative. The IDR has benefited from a solid inflation-fighting period by Bank Indonesia (BI), a sustained current account surplus and an improved growth outlook, helped in part by its strong commodity endowments that mean it should benefit from the global energy transition and demand for electric vehicle batteries, which is becoming a new source of growth.

The correlation of the Vietnamese dong is also close to zero so far this year. The VND, however, is a heavily managed currency unit and has shown no signs of following the CNY during its recent slide. That is simply a local policy decision. And at some point, it may re-set.

Perhaps more surprisingly, the Taiwan dollar also seems to be shaking off any CNY influence and has been notably less responsive to movements in the CNY than past history would suggest. This may be due to portfolio inflows into Taiwan's stock market, as investors seem keen to buy almost any stock with even a vague hint of AI or semiconductors in their business description right now.

Taiwan's stock market is up almost 22% year-to-date as a result, while China's CSI 300 is virtually flat in local currency terms, and down 4.1% in USD terms.

Looking ahead

At some stage, there is a chance that the Chinese government will come out with a broader package of support measures than it has done so far, and that will likely see the CNY rally. That said, we aren't looking for a bazooka from the authorities, more of a shot-gun approach of smaller measures, and believe that any uplift may be short-lived.

One-way traffic in the currency is not something the PBoC will want to see either, but we don't believe they will be totally averse to seeing the CNY weaken further if it does so in a controlled fashion, especially as we doubt that they are done with cutting rates just yet. Market forecasters are toying with near-term targets of USD/CNY 7.30 which looks plausible and in line with the 2022 highs. 7.40 would take the CNY into territory that it has not visited since 2007 and seems a step too far at this juncture, though not something we would rule out.

But even 7.30 could drag other Asian FX with it, with the JPY and MYR likely tracking the CNY most closely (subject to any JPY support that may follow a tweak to their yield curve control policy, which we think could happen in July) while the IDR (and even India's rupee) may partly shrug off any such move.

Author

Amrita Naik Nimbalkar

Junior Economist, Global Macro

amrita.naik.nimbalkar@ing.com

Mateusz Sutowicz

Senior Economist, Poland

mateusz.sutowicz@ing.pl

Alissa Lefebvre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@asia.ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Sector Economist, TMT & Healthcare

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials
Marina.Le.Blanc@ing.com

Samuel Abettan
Junior Economist
samuel.abettan@ing.com

Franziska Biehl
Senior Economist, Germany
Franziska.Marie.Biehl@ing.de

Rebecca Byrne
Senior Editor and Supervisory Analyst
rebecca.byrne@ing.com

Mirjam Bani
Sector Economist, Commercial Real Estate & Public Sector (Netherlands)
mirjam.bani@ing.com

Timothy Rahill
Credit Strategist
timothy.rahill@ing.com

Leszek Kasek
Senior Economist, Poland
leszek.kasek@ing.pl

Oleksiy Soroka, CFA
Senior High Yield Credit Strategist
oleksiy.soroka@ing.com

Antoine Bouvet
Head of European Rates Strategy
antoine.bouvet@ing.com

Jeroen van den Broek
Global Head of Sector Research
jeroen.van.den.broek@ing.com

Edse Dantuma
Senior Sector Economist, Industry and Healthcare
edse.dantuma@ing.com

Francesco Pesole
FX Strategist
francesco.pesole@ing.com

Rico Luman

Senior Sector Economist, Transport and Logistics
Rico.Luman@ing.com

Jurjen Witteveen
Sector Economist
jurjen.witteveen@ing.com

Dmitry Dolgin
Chief Economist, CIS
dmitry.dolgin@ing.de

Nicholas Mapa
Senior Economist, Philippines
nicholas.antonio.mapa@asia.ing.com

Egor Fedorov
Senior Credit Analyst
egor.fedorov@ing.com

Sebastian Franke
Consumer Economist
sebastian.franke@ing.de

Gerben Hieminga
Senior Sector Economist, Energy
gerben.hieminga@ing.com

Nadège Tillier
Head of Corporates Sector Strategy
nadege.tillier@ing.com

Charlotte de Montpellier
Senior Economist, France and Switzerland
charlotte.de.montpellier@ing.com

Laura Straeter
Behavioural Scientist
+31(0)611172684
laura.Straeter@ing.com

Valentin Tataru
Chief Economist, Romania
valentin.tataru@ing.com

James Smith
Developed Markets Economist, UK
james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials

suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri

thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors

maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands

marcel.klok@ing.com

Piotr Poplawski

Senior Economist, Poland

piotr.poplawski@ing.pl

Paolo Pizzoli

Senior Economist, Italy, Greece

paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios

maarten.leen@ing.com

Maureen Schuller

Head of Financials Sector Strategy

Maureen.Schuller@ing.com

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@asia.ing.com

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Philippe Ledent

Senior Economist, Belgium, Luxembourg

philippe.ledent@ing.com

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

Inga Fechner

Senior Economist, Germany, Global Trade

inga.fechner@ing.de

Dimitry Fleming

Senior Data Analyst, Netherlands

Dimitry.Fleming@ing.com

Ciprian Dascalu

Chief Economist, Romania

+40 31 406 8990

ciprian.dascalu@ing.com

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content

+44 (0) 207 767 5331

owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM

+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com