

THE END OF CHINESE YUAN BEAR MARKET?



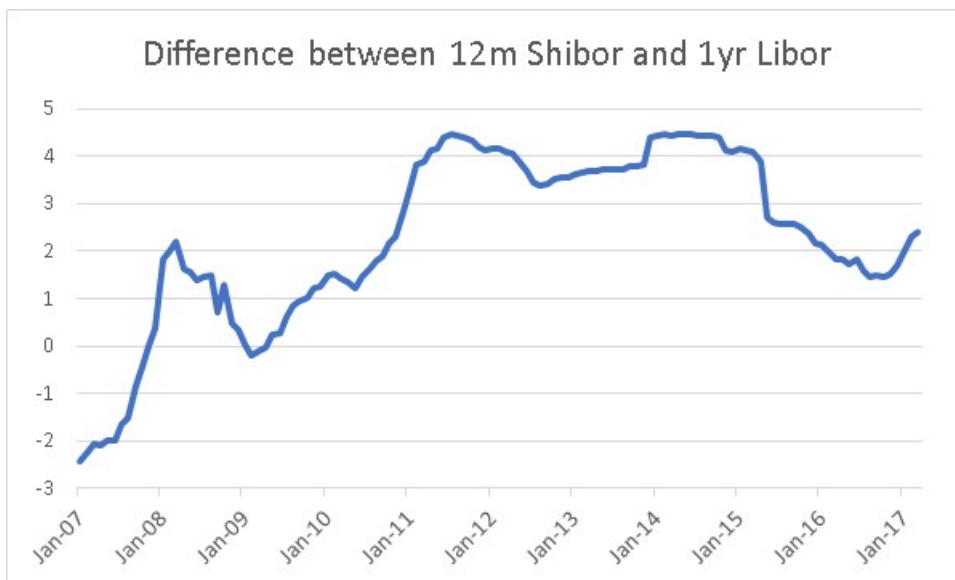
The Chinese Yuan (CNY) was fixed for many years before beginning to appreciate in 2005. Since 2014 it has been in a weakening bias, as the US dollar has been relatively strong.



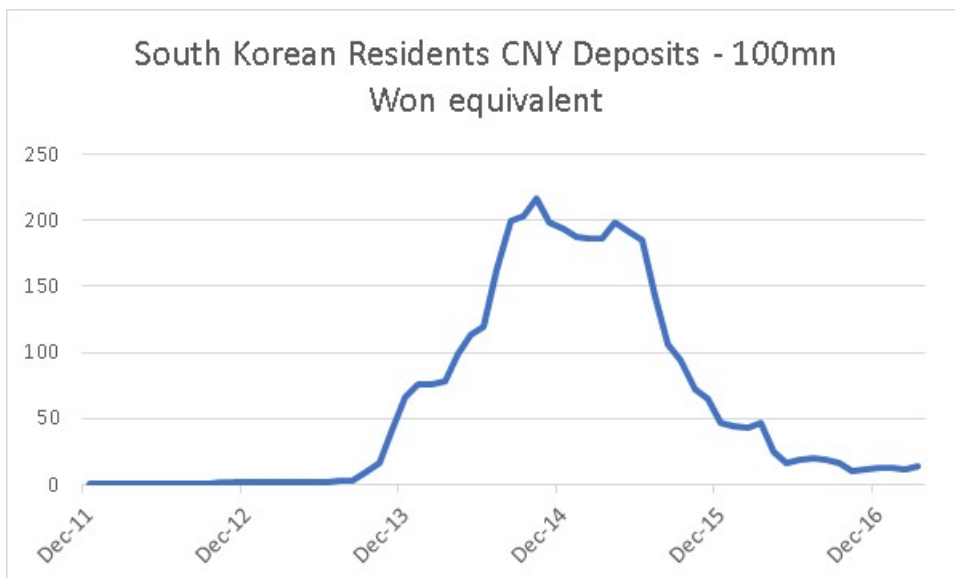
Part of the weakness in the CNY was due to China cutting interest rates from 2015 to help prop up growth. This greatly reduced the relative spread between interest rates between China and the US and put pressure on the currency. (Shanghai Interbank Offer Rate (“Shibor”), London Interbank Offer Rate (“Libor”)).



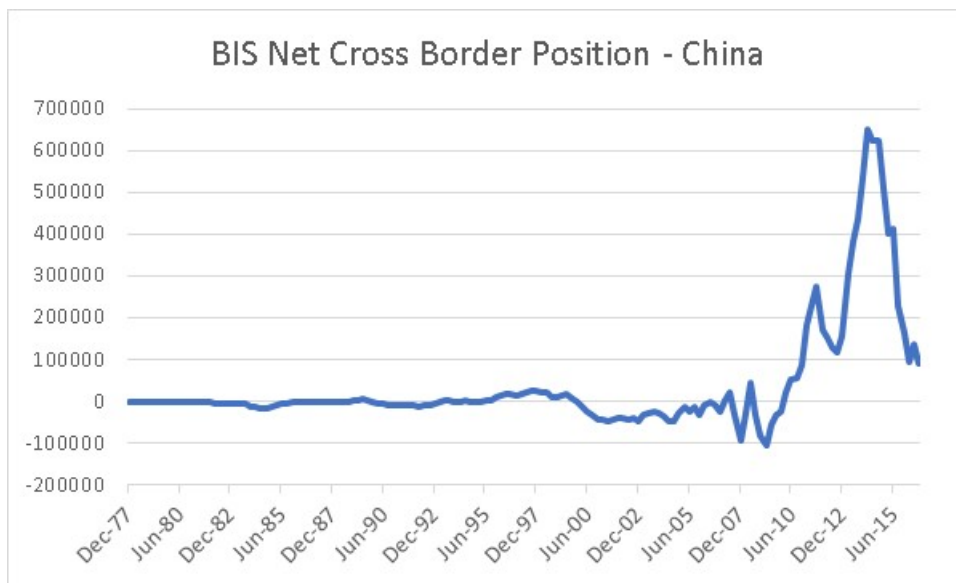
As can be seen the divergence between interest rates is now beginning to move in CNY's favour.



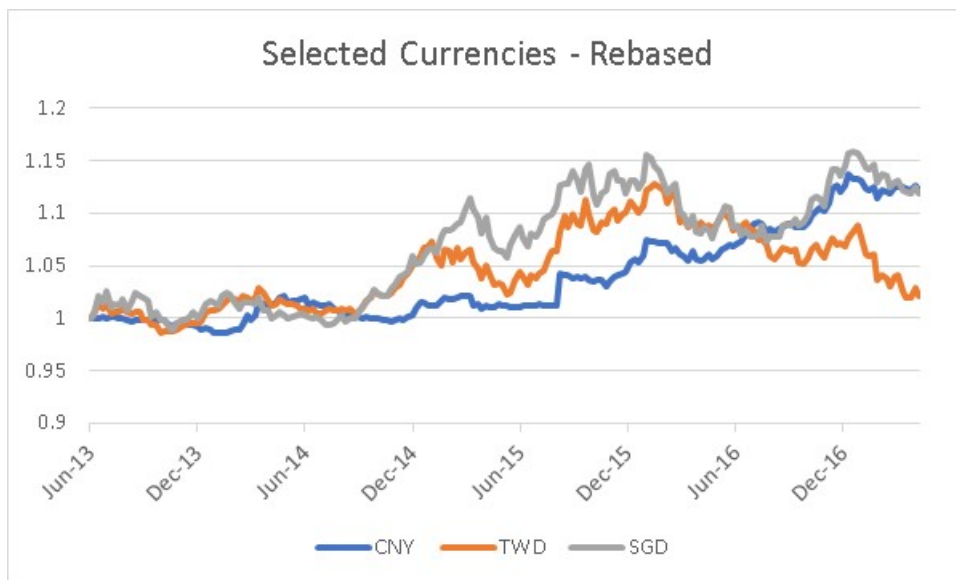
As rates were cut and the CNY weakened, there was a large outflow from both foreigners and locals. One example is the movement out of CNY by Koreans.



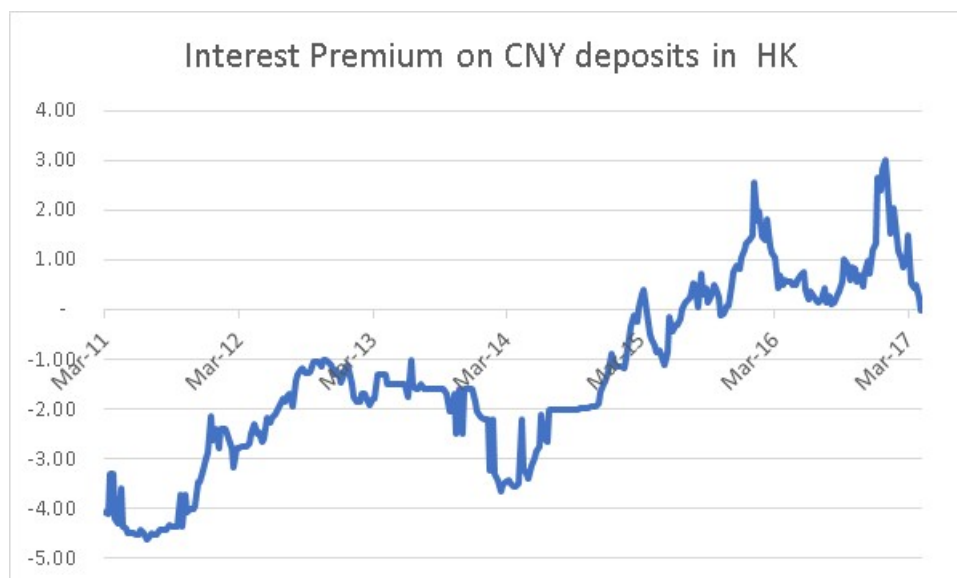
This collapse in foreign exposure to China is confirmed by Bank of International Settlements (“BIS”), although this data is only to q3 2016.



What I find interesting is that the currencies of countries with strong trade links to China, namely Taiwan and Singapore, were good early signals to an imminent Chinese devaluation in 2014. These currencies, and particularly the Taiwanese dollar have strengthened considerably recently.



Intriguingly the interest rate needed for offshore CNY deposits in Hong Kong has fallen below the mainland rate for the first time since 2015.



As can be seen, Hong Kong deposit rates can fall below the mainland rate depending on the locals' view of the CNY exchange rate. Given the reduced positioning of foreigners in CNY, the flattening of the banks' foreign currency positions in Chinese banks, the strengthening of CNY proxy currencies and the implied bullishness of Hong Kong depositors on the CNY, the CNY looks more likely to appreciate than depreciate from here.

INFORMATION

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