



Chinese yuan

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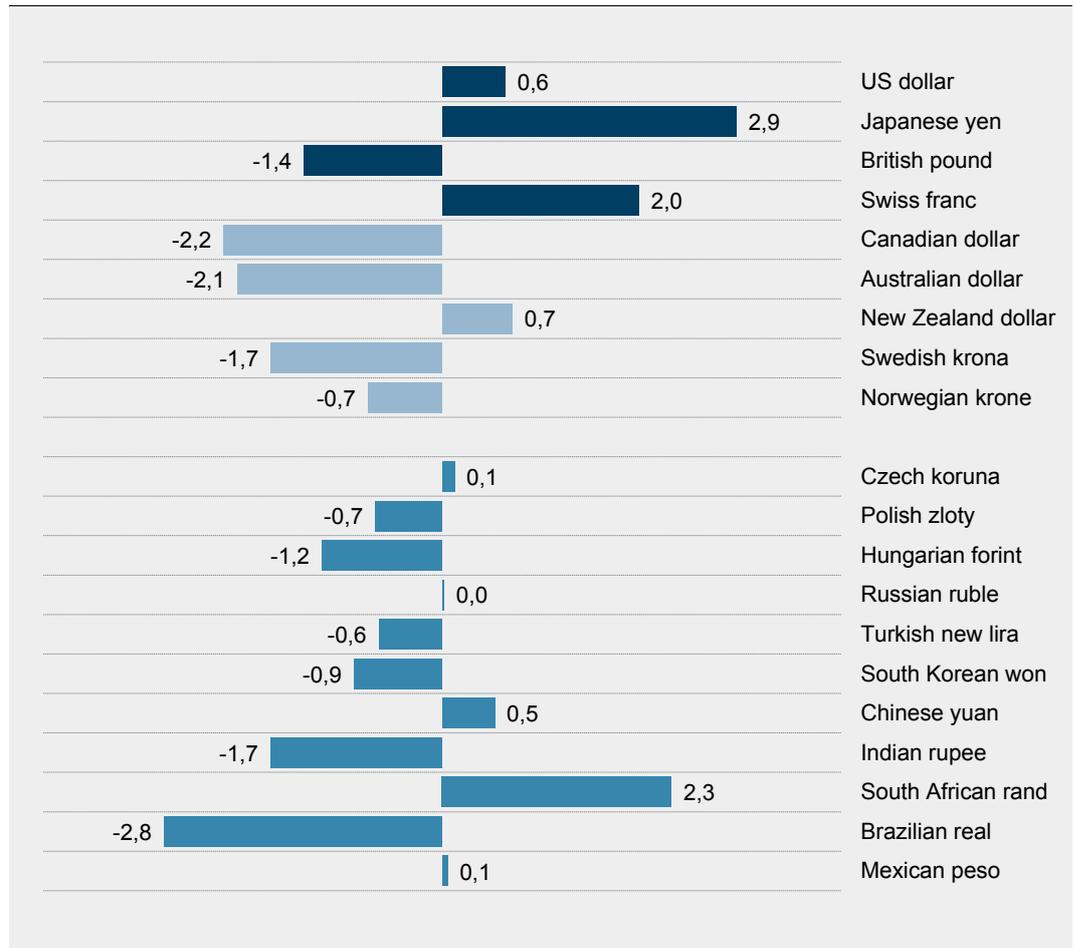
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- The US dollar was able to recover a little most recently. The Japanese yen and the Swiss franc advanced strongly. With the exception of the stronger South African rand, commodity and emerging market currencies tended to come under pressure.
- The Chinese yuan was able to end its slump, and since 2017 it has advanced noticeably against the US dollar. In addition to the higher growth in China, the exchange rate policy is likely also playing an important role. The stronger euro in a sense pulled the yuan along. However, the tailwind for the yuan should wane in 2018. It should weaken somewhat against the US dollar, though it will presumably appreciate a little against the euro.
- Helaba Currency Forecasts

Performance on a month-over-month basis

% vs. euro compared to the previous month (from 01/24 to 02/22/18)



■ Core currencies ■ Rest of G10 ■ Currencies of emerging markets

Sources: Bloomberg, Helaba Research

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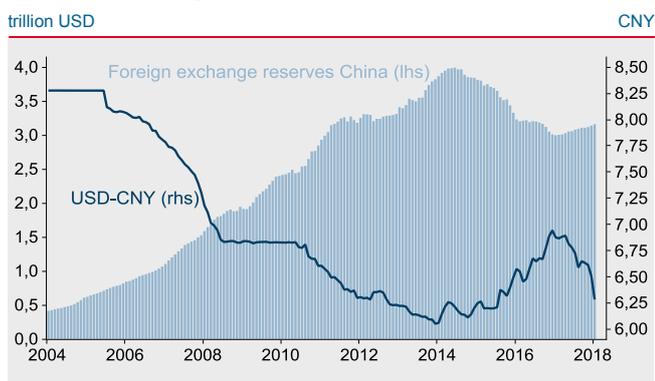
CNY: momentum weakening

The Year of the Dog has begun, what is generally linked with good virtues. Does that apply to the Chinese currency? Two thousand seventeen, the Year of the Rooster, already proved surprisingly positive for the Chinese yuan. China's currency ended an approximately three-year slump and gained more than 8 % against the US dollar. However, a clear loss remained against the euro.

Capital flight at an end?

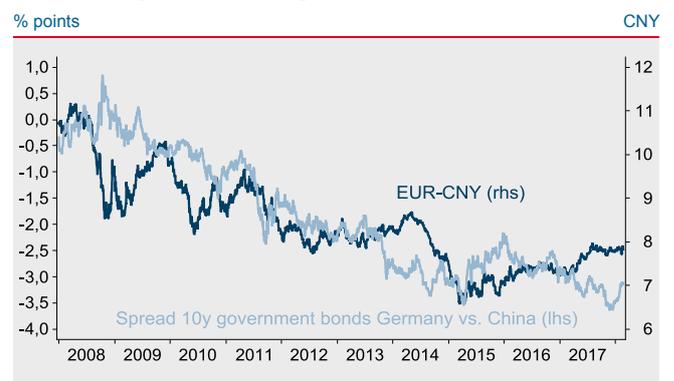
Concerns about the economic development in China contributed to the depreciation of the yuan between the beginning of 2014 and the end of 2016. Capital, both domestic and foreign, was taken out of the country. Evidence of that were the noticeably shrunken currency reserves of China's central bank. By now, the reserves have stabilized again or are even growing slightly. Accordingly, the capital flight must have come to an end. The fears about China's growth have abated. The economic slowdown of the previous year did not continue in 2017, as GDP grew by 6.9 %.

China's currency reserves have stabilized



Sources: Macrobond, Helaba Research

Yuan with yield advantage over the euro



Sources: Macrobond, Helaba Research

Economic momentum slowing again

The robust growth rested not least of China's stimulatory economic policy. In addition to higher government spending, lending, in particular, was boosted. By now, however, the government is taking its foot off the gas, since indebtedness of companies and consumers is being increasingly recognized as a problem. As a result, the economic momentum should weaken in 2018. GDP will presumably come in at only 6.5 %. While this means that major concerns are not necessarily called for, at least the tail wind is slowing.

Reduced government promotion of growth in lending does not automatically suggest significant increases in interest rates. As it is, the key rate does not play in China the major role as it does in other countries, moreover, the very moderate inflation does not pose a problem. To be sure, Chinese bond yields are tending to rise. However, the yield advantage over the US has shrunken noticeably in recent months, as a result of which the yuan has, in relative terms, lost attractiveness. Against the euro, China's interest rate advantage shrank only over the last few weeks, in 2017 it increased overall.

Politics is "Trump"

Classic fundamental factors have only a limited explanatory power when it comes to the yuan. The exchange rates continue to be strongly influenced by the Chinese government, even if the reins have been loosened a little with respect to the daily fixings. The question that arises is which exchange rate targets the politicians are currently pursuing, and whether US President Trump is even influencing them. Donald Trump has been criticizing China's trade policy for a long time. Among other things, he accused China of keeping the currency artificially low to boost exports. However, the US government continues to shy away from officially branding China as a currency manipulator – courtesy of the North Korea crisis! In any case, that accusation was not justified, at least over certain stretches, since the Chinese tended rather to fight against an excessive depreciation. Perhaps China is trying to appease Trump somewhat with the slight yuan appreciation since 2017. However, that is not keeping the US president from increasing tariffs on

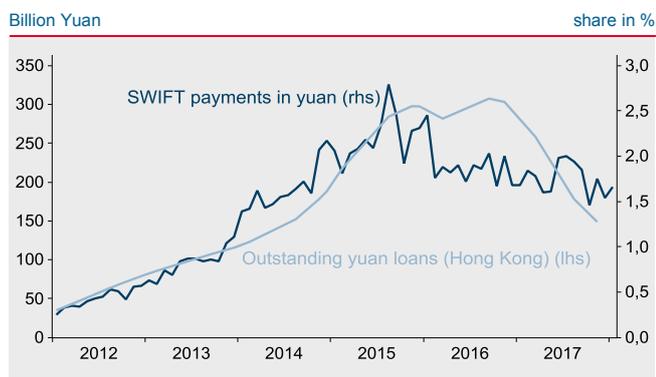
solar panels, washing machines, and in the near future probably also steel. Surely, this is a long way from the trade war with China that Trump proclaimed during the campaign, but the pin-pricks are multiplying. Principally, however, there is reason to doubt whether the Chinese government is still paying any special attention on foreign feelings at all when it comes to its exchange rate policy. Thus a massive yuan depreciation seems hardly probable as retaliation with respect to trade policy. Likewise, China is not likely to divest itself on a larger scale of its holdings of Treasuries out of a concern about US deficits. After all, the country would also cause itself financial and economic harm by doing so.

The attempt to establish the renminbi as a new global currency or even replace the US dollar is running into limits for now. To be sure, it was officially added to the currency basket for the special drawing rights of the International Monetary Fund. By now, large central banks – among them the Bundesbank – hold the Chinese yuan as a reserve currency. Outside the political realm, though, the yuan continues to wait for its breakthrough. The yuan has rather lost shares in the international payment transactions. The Chinese currency has not been able to follow up its initial successes in the international markets with respect to bond issues and customer deposits. The road to developing the yuan into one of the world’s leading currencies is still a very long one.

Yuan without a clear inaccurate valuation

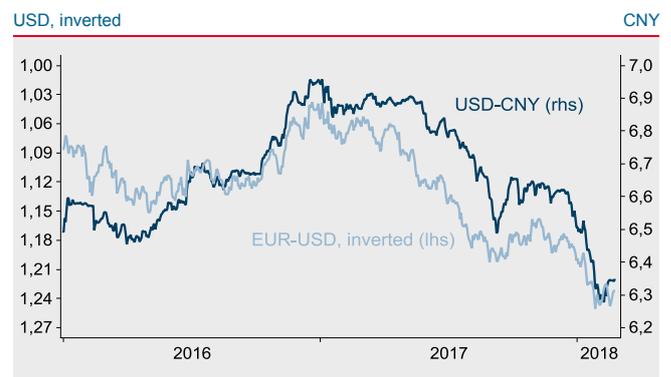
China’s current account surplus shrank noticeably already a few years ago and has settled on the usual level of around 2 % – as measured in terms of GDP. This does not point to a clear inaccurate valuation of the yuan’s external value. A “fair” value of the yuan is difficult to derive, given a national economy that has been changing strongly over many years, especially since historically the exchange rates were largely managed by the government. The currency is trading below its trade-weighted highs of 2015, though not at a low level.

Yuan losing importance again internationally



Sources: Macrobond, Helaba Research

Rising euro depresses dollar-yuan exchange rate



Sources: Macrobond, Helaba Research

Slight gains against the euro, slight losses against the US dollar

Another aspect is China’s attention to the trade-weighted external value. When the euro appreciates against the US dollar, the yuan in turn loses against the euro. In order to keep the Chinese currency basket fairly stable, the yuan must therefore appreciate slightly against the US dollar. And in fact, since the beginning of 2017 – as well as frequently also during other phases in the past – one can see this connection: the euro-dollar exchange rate rises, the dollar-yuan exchange rate declines a little. We believe that the euro rise against the US dollar was exaggerated, which means that the exchange rate is likely to correct again in the coming months. As a result, the yuan will probably also weaken a little against the US dollar. The dollar-yuan exchange rate will presumably rise to 6.5. But this implies a slight yuan appreciation against the euro, and the euro-yuan exchange rate could fall from 7.8 most recently to 7.50. As such China’s currency will surely not be going to the dogs, but against the US dollar the Year of the Dog will not be able to keep up with the Rooster.

Helaba Currency Forecasts

	Performance			Forecast horizon at end ...			
	year to date	1 month	current*	Q1/2018	Q2/2018	Q3/2018	Q4/2018
vs. Euro	(vs. Euro, %)						
US dollar	-2,6	0,6	1,23	1,20	1,15	1,15	1,20
Japanese yen	2,8	2,9	132	132	125	125	128
British pound	0,5	-1,4	0,88	0,85	0,90	0,90	0,85
Swiss franc	1,7	2,0	1,15	1,12	1,15	1,17	1,15
Canadian dollar	-3,7	-2,2	1,57	1,54	1,50	1,47	1,51
Australian dollar	-2,2	-2,1	1,57	1,54	1,49	1,47	1,50
Swedish krona	-1,7	-1,7	10,01	9,50	9,40	9,20	9,00
Norwegian krone	1,6	-0,7	9,68	9,10	9,00	8,90	8,80
Chinese yuan	-0,5	0,5	7,84	7,68	7,48	7,48	7,68
vs. US-Dollar	(vs. USD, %)						
Japanese yen	5,6	2,3	107	110	109	109	107
Swiss franc	4,4	1,3	0,93	0,93	1,00	1,02	0,96
Canadian dollar	-1,1	-2,8	1,27	1,28	1,30	1,28	1,26
Swedish krona	0,8	-2,3	8,12	7,92	8,17	8,00	7,50
Norwegian krone	4,5	-1,3	7,85	7,58	7,83	7,74	7,33
Chinese yuan	2,4	0,1	6,35	6,40	6,50	6,50	6,40
US-Dollar vs. ...	(vs. USD, %)						
British pound	3,3	-2,0	1,40	1,41	1,28	1,28	1,41
Australian dollar	0,5	-2,7	0,78	0,78	0,77	0,78	0,80

*22.02.2018

Sources: Bloomberg, Helaba Research ■