

# Market Watch

## US reacts to Yuan move

### Summary

- **US labels China a currency manipulator in response to USD/CNY breaking above 7.00 yesterday**
- **S&P500 fell almost 3%, 10-year US Treasury yield moved below 1.70% (from 1.84%) and USD/JPY fell below 105.80 (from 106.59).**
- **Market re-assessment process may not yet be complete. Any further reaction from China is now key.**

### Background

USD/CNH broke above the key 7.00 level yesterday. Following this move, the US formally labelled China a 'currency manipulator', with the US Treasury saying "in recent days, China has taken concrete steps to devalue its currency, while maintaining substantial foreign exchange reserves despite active use of such tools in the past." This also follows reports Chinese companies had stopped buying US agricultural products.

### Reaction

Global equities fell 2.5%. Asia-ex Japan equities fell 3.1% yesterday while, overnight, Euro Stoxx 600 fell about 2.3% and the S&P500 fell about 3.0%. The 10-year US Treasury yield fell below 1.70%, USD/JPY moved below 105.80 while gold rose to USD 1464. The US 10yr-3m yield gap (a commonly followed recession indicator) fell to its lowest negative level since 2007.

### What does this mean for investors?

We believe markets are considering three possible scenarios, monitoring of which could help chart the path forward.

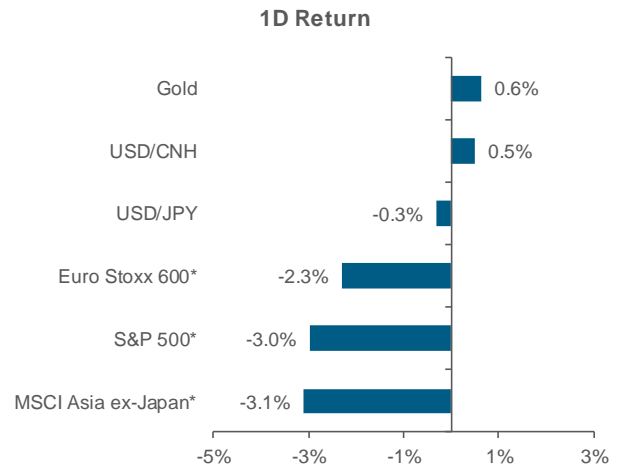
- First is whether recent moves are merely a "tit-for-tat" response, or mark a more significant trade-war escalation. China's reaction will be key. Major signposts include whether today's USD/CNY policy fix stays below 7.00 and whether China reaches for other escalatory tools (such as additional tariffs or the 'unreliable entities' list) in the coming days.
- Second is whether Yuan weakness also involves an effort to support growth. Incoming economic data can offer guidance, but we would also keep a watch for any signs of excessive capital outflows, a risk during prior periods of Yuan weakness.
- Finally, we would also monitor the extent to which US actions raise pressure on the Fed to cut rates further. Market pricing of Fed rate cuts suggest chances of further rate cuts are rising.

### What are key technical levels to watch?

We plot distance to key support (or resistance) levels for key asset classes in the chart on the right. Some major equity markets are now close to a key support level. While these levels may hold if there is no further escalation, any break opens up the risk of a renewed fall to Nov-Dec lows, 8-10% lower from current levels.

### Equities fall after yesterday's FX market moves

Performance of selected asset classes on 6 August 2019



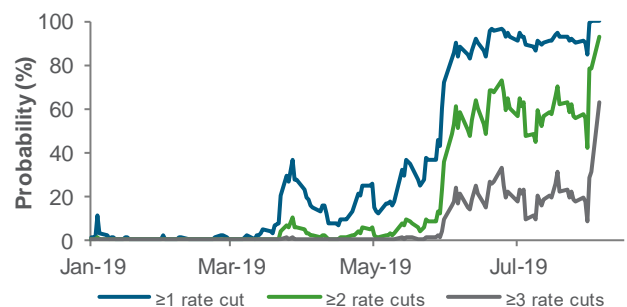
Source: Bloomberg, Standard Chartered

As of 6 August 2019, 7:50am SG time

\*Returns calculated based on 5 August's close

### Markets now pricing a high likelihood of 2-3 further 25bps Fed rate cuts by year-end

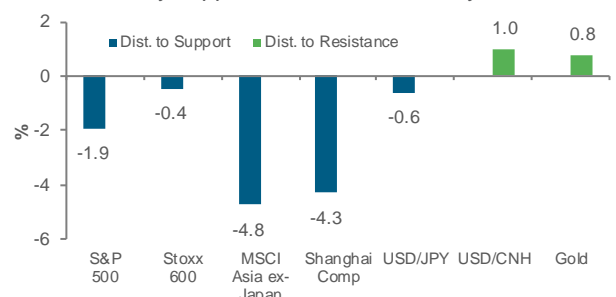
Probability of rate cuts (%) based on Fed Fund Futures



Source: Bloomberg, Standard Chartered

### Major markets not far from next key technical level

Distance to key support or resistance for key markets



Source: Bloomberg, Standard Chartered

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