

# Market Watch

## USD/CNH breaks 7 on tariff response

### Summary

- **USD/CNH broke above psychological resistance at 7.00.**
- **PBoC comments directly linked depreciation of the Yuan with trade protectionism and tariffs on Chinese goods.**
- **Monitor key signposts for severity and length of impact**

### Background

On Thursday 1<sup>st</sup> August, US President Trump unexpectedly announced a 10% tariff on an additional USD 300bn of Chinese products (effective 1<sup>st</sup> September), a day after the US Federal Reserve cut its benchmark interest rate by 25 bps. China's UN ambassador said on the following day that the country would take "necessary counter-measures" to protect its rights and further suggested that escalating trade tensions could hurt broader global cooperation, particularly referencing North Korea.

Today, USD/CNH rose above the 7.00 mark for the first time since the offshore Chinese yuan (CNH) was introduced amid a rise in the USD/CNY policy fixing rate to 6.9225. China's central bank comments emphasised that the currency could be kept "absolutely stable", but that the FX market "can find its balance on its own".

### Reaction

The offshore USD/CNH rallied to a high near 7.1080 intraday, with the onshore USD/CNY touching 7.03. USD/JPY fell to a low of 105.80 and gold rallied above the July high at 1452, touching 1455. Asian currencies were broadly weaker, with USD/KRW at its highest level since March 2016, and USD/INR up more than 1%. The US Treasury 10-year yield fell to a 39-month low at 1.76%.

### What does this mean for investors?

We believe there are three key signposts to watch from here that could help define whether the currency move is merely a "tit-for-tat" response to proposed new tariffs, or an escalation of the US-China trade war that may also trigger further geopolitical stress:

- any response from the Trump administration to CNY weakness,
- onshore USD/CNY policy fixing levels in the coming days, and
- Japanese officials' words and/or action in the face of JPY gains.

Escalation of tensions over trade, Hong Kong unrest, Iranian naval actions and North Korean missile testing are possible. We remain constructive on risky assets on a 6-12 months horizon, but as our H2 Outlook flagged, volatility could rise over the next 3 months.

### What are key technical levels to watch?

- USD/CNH resistance at 7.20 – 7.25 (that approximates some estimates of CNY weakness required to offset new tariffs)
- USD/JPY important support between 104.50 – 105.00
- MSCI Asia ex-Japan Index support at 612 (about -1.0%)
- Hang Seng Index support at 24,540 (about -6.2%)
- MSCI All Country World Index support at 491 (about -4.5%)

### Safe-havens benefit following tariffs, CNH weakness

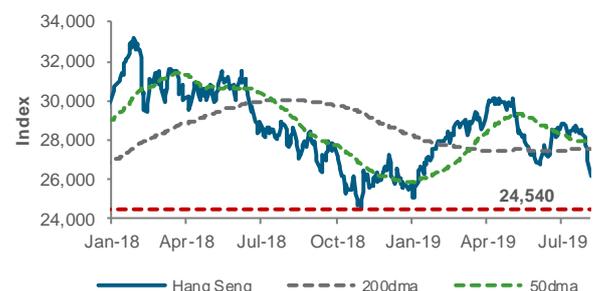
Performance of selected asset classes on 5 August 2019



Source: Bloomberg, Standard Chartered  
As of 5 August 2019, 3:30pm SG time

### Trade and political tensions hurt HK equities

Hang Seng Index (daily) with technical levels



Source: Bloomberg, Standard Chartered

### PBoC comments link currency weakness to trade

USD/CNH (daily) with technical levels



Source: Bloomberg, Standard Chartered

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