

Chinese renminbi

	Spot close 31.01.20	Q1 2020	Q2 2020	Q3 2020	Q4 2020
USD/CNY	6.9300	7.1000	7.0700	7.0500	7.1200
USD/HKD	7.7657	7.7800	7.7700	7.7700	7.7600
		Range	Range	Range	Range
USD/CNY		6.8350-7.1500	7.0000-7.1500	6.9500-7.1500	7.0000-7.2000
USD/HKD		7.7600-7.8000	7.7600-7.8000	7.7600-7.8000	7.7500-7.8000

MARKET UPDATE

Flat; MLF down 5bp

By dint of a delayed market re-opening, the 23 January close became the official month close at 6.9300, compared with a London close of 6.9662 in December. But the CNH, which traded during Chinese New Year, closed at 6.9988. PBOC cut RRR and then MLF by 5bp, but held LPR (which we had expected).

OUTLOOK

We lay out working assumptions on the economic impact of coronavirus

It's been a traumatic January. We know traumatic in Markets will have been, in scores of cases, personally tragic for many families in China so our sympathies go out to them. We are not the economists *per se* in this Bank, but since FX outlooks should be based in part on macro – perhaps none more so than this month – we need to state clearly our working assumptions about the economic impact of the novel coronavirus that has hit China.

Early medical and epidemiological evidence suggest to us this epidemic will be worse than SARS

We are assuming the Wuhan coronavirus will ultimately be a more severe epidemic than SARS. We say this because it appears to be much more contagious than SARS. SARS infected 8,098 people. Epidemiological models at Imperial College in London are suggesting an ultimate toll in the range of 30,000-200,000. Other public health experts have spoken of a million. These #s depend critically on how many people each carrier infects (initial studies suggest 2-4) and how successful are government quarantine and control efforts. While initially Wuhan mortality appears lower than SARS, we think an adjustment for final death rates (current proportions are biased downward due to truncation) will narrow the mortality experience with SARS, which saw a little less than 10% die. If #s of infections stop at 100,000 and we use a scaled-up estimate of 6% for the death rate, we could be looking at 6,000 to 7,000 deaths, making this epidemic of an order of magnitude larger than SARS (which killed less than 800 people). It's a natural inclination to ignore unpleasant news, at least initially, but a widespread infection coupled with dangers of death will inhibit economic activity through both government quarantine and control and sensible self-precautions by individuals, households and firms (leading to people not congregating, thereby inhibiting normal economic activity). Like SARS, this natural disaster is primarily a demand shock.

We foresee a possible -1 to -2ppt hit to 2020 Chinese growth

Past studies of SARS suggested it took 1ppt off of Chinese growth. Because this epidemic may be larger, **we assume a -1 to -2ppt shock off of growth for China in 2020.** Most of this occurs in 1H20 (there should be a rebound in 2H), when experts suggest infections peak in late April or early May (as warm weather returns). It's a shorter duration event than SARS (which lasted nine months) because of greater Chinese transparency and efforts to contain the spread. But as China is now far larger and more integrated into the world economy, we can also expect knock-on effects for many economies (and not only in the region).

	Interest Rate Close	Q1 2020	Q2 2020	Q3 2020	Q4 2020
Loan Prime Rate1Y	4.15%	4.00%	3.85%	3.70%	3.55%
MLF 1Y	3.20%	3.10%	3.00%	2.90%	2.80%
7-Day Repo Rate	2.60%	2.75%	2.75%	2.75%	2.75%
5-Year Yield	2.79%	2.95%	2.95%	2.95%	2.95%

* Interest rate assumptions incorporated into MUFG foreign exchange forecasts.

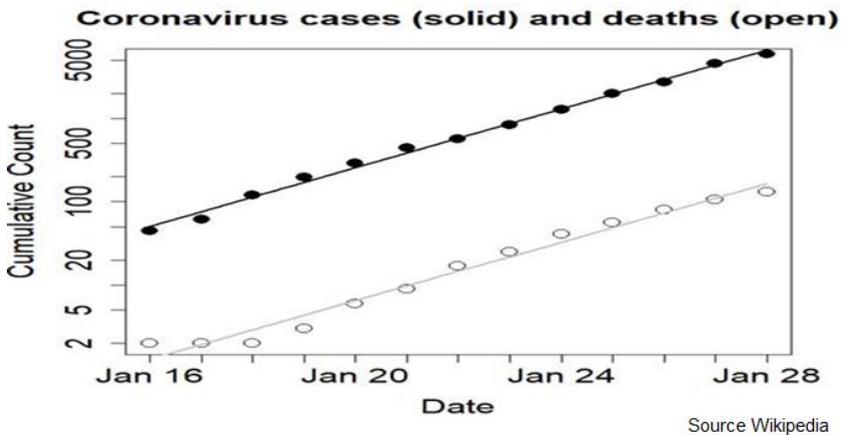
INTEREST RATE OUTLOOK

This presses PBOC to reduce rates and yields faster

The PBOC had been on an ongoing quest, we thought, to lower rates and yields even further, given this year's herculean refinancing task. Slower prospective economic growth will motivate it to do so more urgently, not least of which because refi becomes harder. Whether such efforts exactly coincide with the eventual decline of pork prices may be less important, so are more forced in our forecasts. An event like the coronavirus should normally lead to a buy on govies and a short on credit, if Markets are decisive. Because we have discussed possibility of a side currency agreement with Team Trump to strengthen the renminbi (at least in trade-weighted terms), China will again take on the impossible trinity by seeking lower interest rates but a stronger currency.. A wild card is capital flows; we would not be surprised if capital controls are re-tightened at this stage. There were a bevy of companies with pressing repayments over Chinese New Year as we went to press. If any of them defaulted over the holidays, we won't know till after the now extended break ends.

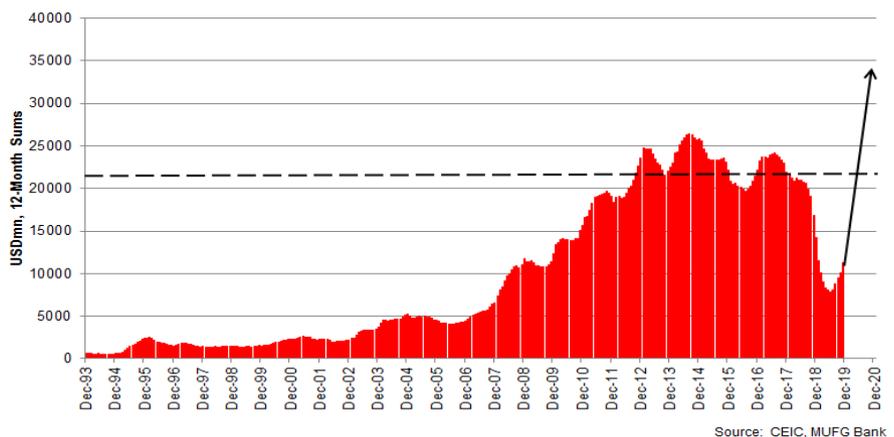
Following a geometric trend in early stages

INITIAL INFECTION, DEATH STATISTICS FOR THE WUHAN CORONAVIRUS



The Chinese committing to all-time records

TOTAL VALUE OF ALL CHINESE AG IMPORTS FROM THE US



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