

Chinese renminbi

	Spot close 28.06.19	Q3 2019	Q4 2019	Q1 2020	Q2 2020
USD/CNY	6.8683	6.8500	6.9200	6.8500	7.0000
USD/HKD	7.8106	7.8000	7.7900	7.7850	7.7750
		Range	Range	Range	Range
USD/CNY		6.7500-6.9500	6.8500-7.0000	6.7500-6.9500	6.8500-7.0500
USD/HKD		7.7800-7.8300	7.7700-7.8200	7.7700-7.8200	7.7600-7.8100

MARKET UPDATE

Stronger, anticipating Truce; PBOC husbanded liquidity carefully in June

A Trump Tweet confirming his meeting with Xi Jinping at the Osaka G-20 saw a relief rally that sent USD/CNY lower, finishing at 6.8683 though it earlier climbed above our 2Q19 forecast of 6.92, down from May's London close of 6.9020. PBOC managed liquidity carefully, onshore rates softened and a worrisome end-of-month yield spike was avoided.

OUTLOOK

We do not believe Trump has turned over a new leaf on Trade

Has Donald Trump turned over a new leaf with regard to beliefs and intentions on global trade following the Osaka G-20? **No.** Only days after his 73rd birthday, Trump's core Mercantilist trade beliefs, as we have been discussing since December 2016, are what they are. At this stage, we think each Trump move is calibrated toward him winning re-election in 2020, even the concessions he made to China in Osaka. There may be many who look at his actions at the G-20 as a Cave. Maybe. For now. For this mercurial US President we can also believe this will be his maximal concession and that this will lead to more Trouble in Paradise going forward, as we experienced from February-April.

Markets very likely to turn risk-on after the G-20 weekend, good time to hedge

Markets are likely to turn risk-on following the Truce resumption. This is consistent with trading patterns before and after the Buenos Aires dinner. But we think reaction will be less this time since some of it was anticipated before the Xi-Trump Lunch. As typical, equities should rally more than currency (and encourage Trump that his concessions were a good move, for him). Our guidance on currency is to wait for a dip and then hedge.

Huawei may be off the hook, but we really don't know

Trump's concessions on Huawei were his most startling and puzzling. For China, it appeared mission partially accomplished on what had been their most important demand. As sometimes is the case with Trump, who spent more time spinning the meeting at the press conference than for the meeting itself, few people seemed certain what he intends.

Trump did seem desperate to boost US farm sales to China

What the US chiefly secured from China were promises of significant agricultural buys (though China declined to confirm); in fact, Trump seemed almost desperate to boost US farm sales to China (in his first year in office, during the fiscal year that ended in September 2017, the US sold USD22bn of agricultural goods to China, its #1 ag market). We can imagine internal polling done by the Republican National Committee which is running Trump's campaign showing he could be losing in key agricultural states and so advised doing something, anything *now*.

The Chinese economy will not stabilize in 1H19

Official PMIs released the day after the Truce confirmed the economy will *not* stabilize in 1H19; this is a worse outcome than we anticipated. Given the way car sales have tanked, we wonder if Chinese consumer estimates of *permanent income* have decreased.

	Interest Rate Close	Q3 2019	Q4 2019	Q1 2020	Q2 2020
Policy Rate	4.35%	4.35%	4.35%	4.35%	4.35%
7-Day Repo Rate	2.63%	2.50%	3.00%	3.00%	3.00%
5-Year Yield	3.05%	3.00%	3.20%	3.10%	3.30%

* Interest rate assumptions incorporated into MUFG foreign exchange forecasts.

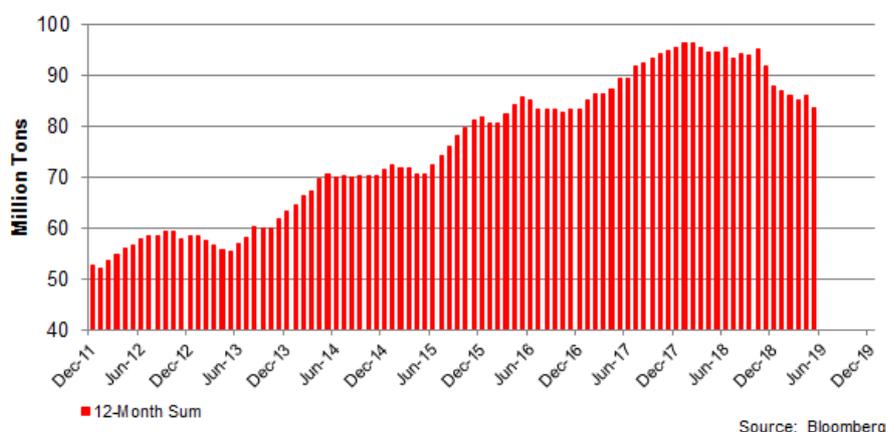
INTEREST RATE OUTLOOK

Why does this economy keep needing stimulus?

Economic weakness means more EMS – not emergency medical services but Even More Stimulus. There remain plentiful expectations onshore for more interest rate and RRR cuts, and July is due for a Targeted MLF injection (rate cuts in China, by the way, will dull the impact of future Fed cuts). MUMSS colleagues expect a further spike in the quota for special local government bond issuance. And ongoing Credit Deterioration – our other candidate for sharply higher USD/CNY forecasts – proceeds apace. The Boshang Bank takeover constrained funding for city commercial banks heavily dependent on the interbank market. Small securities firms who bought some of these bank NCDs found they could not pledge them as collateral for more funding, unless they were willing to pay interest rates of upwards of 15%. More seriously, China’s 9th largest bank faces a US Appeals Court “death penalty” of being cut off from the USD funding system. Should we be proved wrong and Trump has indeed dialed down the temperature of Future Trade Wars, we note that must also imply less of a reason for the Fed to cut.

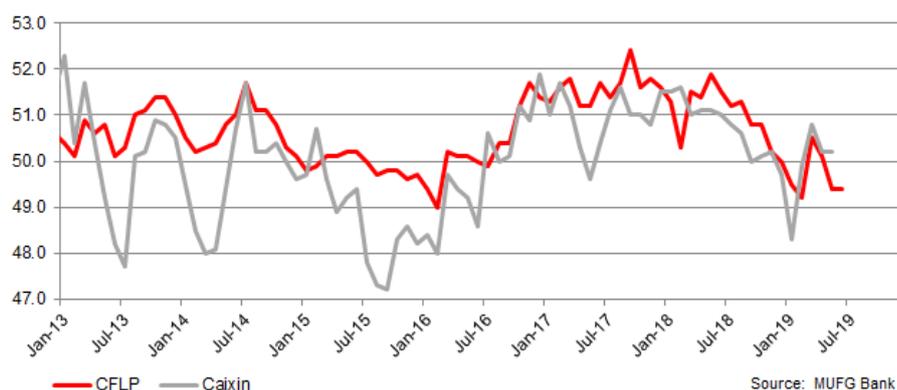
Sales keep dipping

US EXPORTS OF SOYBEANS TO CHINA



Not stable yet

CHINA: MANUFACTURING PMIS



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