

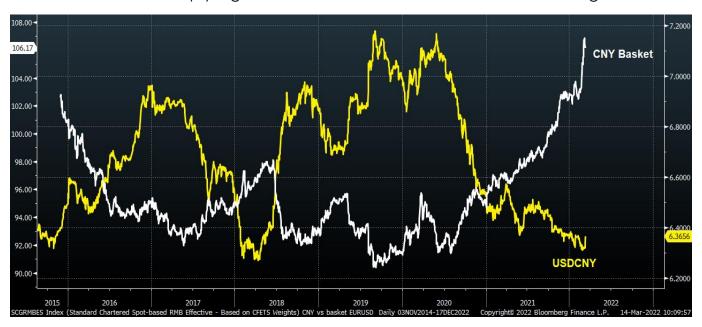
## MI2 Trader: CNH

14th March 2022

## Comment

In contrast to the 2008 Olympics, which marked China's triumphant ascension to economic superpower status, events since the start of the Winter Olympics have been inauspicious, to say the least. Not only is the Middle Kingdom grappling with weakening GDP and a precarious property market, but it now faces a massive acceleration in Covid, which, if Hong Kong is any guide, could get utterly out of control. And if that wasn't enough, China has been placed in an untenable diplomatic situation by its best buddy Russia. This situation is finally forcing international equity investors to stare in the face the risk of a new Cold War and its potential to massively add to the pain in domestic equity markets.

Yet, throughout these developments, the CNY has been a bedrock of strength, accelerating markedly since mid-2021 vs the USD and the broad basket. We suspect this move has a lot to do with the PBoC's attempts to protect the economy from imported inflationary pressures. Indeed, as the EUR (and now JPY) have weakened, the Renminbi basket has moved sharply higher and is now 15% above its mid-2020 average.



Yet, with GDP falling and deflationary pressures building in not only domestic but international equities, how long can and should the PBoC keep this stance up? In fact, with the likelihood of monetary easing coming back into view, reversing some of this unwanted currency strength would be a natural corollary of that monetary policy stance.

## **Trade**

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Buy spot USDCNH here just below 6.40, with a stop at new lows and target  $\sim$ 6.80 for a 4:1 trade with a little negative carry. Alternatively, with our bias to run long the tails in a volatile world, a 25 delta 3-month USDCNH call with ATM vol around 4.5% even with a little bit of skew to the topside looks attractive to us.



PS. While it depends on how the PBoC chooses to manage the CNY move vs the basket, a move higher in USDCNY would be consistent with EURUSD strength.



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