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# CAN CHINA'S CURRENCY CONTINUE ITS BULL RUN?

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China's currency has been on a strong bull run against the US dollar since 27 May 2020. Since then, the renminbi is up almost 11%<sup>11</sup> relative to the greenback. This is especially noteworthy given other currencies in the emerging markets universe, such as the Russian ruble or the Mexican peso, have not demonstrated similar gains. The story, therefore, is not merely one of dollar weakness. We outline the key forces influencing the currency's trajectory.

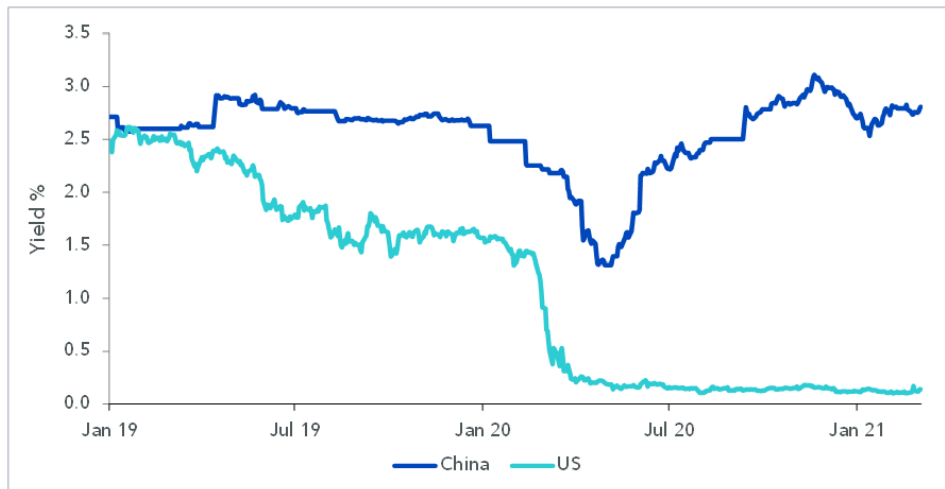
## Ties with the Biden administration

China received considerable ire from the Trump administration over its currency. While it would be premature to assume that trade tariffs will diminish or disappear imminently, China's relationship with the new administration may be more orderly. Might China allow its currency to remain strong or get stronger still in a bid to improve bilateral ties? If that happens, policy intervention could take a back seat, and market forces could operate unabated.

## The lure of a higher yield

Chinese government bonds offer meaningful yield pickup relative to other major economies (see figure 01 below). The combination of China liberalising its capital markets and higher relative yields bodes well for the flow of foreign funds into the country. Chinese government debt is increasingly being added to notable bond indices – with the expected inclusion in FTSE Russell's World Bond Index later this year being a noteworthy highlight. And if the US dollar remains weak, investors will be incentivised further to hold or purchase renminbi denominated assets.

**Figure 1: 2-year government bond yields have diverged significantly**



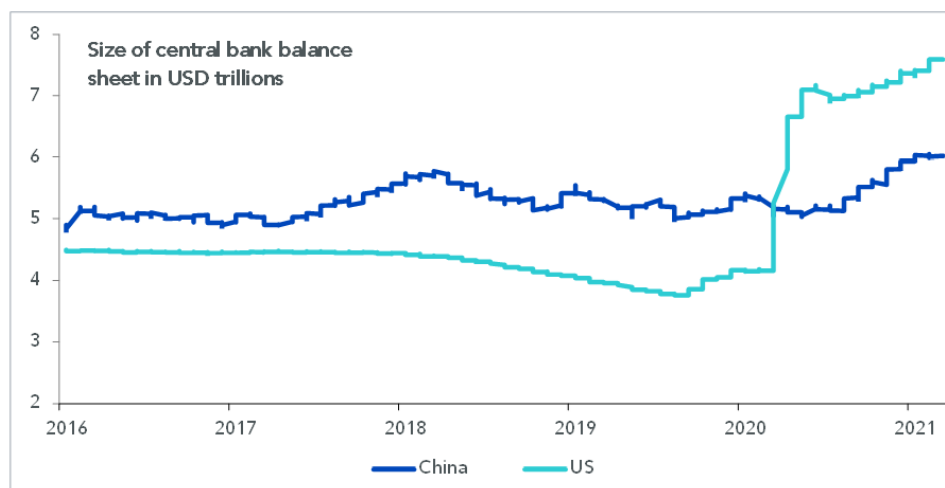
Source: Bloomberg, data as of 04 March 2021. Using Generic China 2 Year Government Bond (GTCNY2Y) and Generic US government Bond 2 Year Yield (USGG2YR).

**Historical performance is not an indication of future performance and any investments may go down in value.**

**US monetary policy largesse may continue**

Money supply from the US Federal Reserve (Fed) has reached record highs since the pandemic last year. While the People’s Bank of China has also been accommodative, its dovishness appears relatively subdued in comparison (see figure 02 below). The Fed has recently reiterated its accommodative policy stance despite rising inflation expectations in the US. While China’s central bank may not necessarily turn hawkish this year, its position may be less dovish than that of the Fed, given its economy has experienced a much stronger and swifter recovery than the US. This could keep the pressure on the US dollar.

**Figure 2: Central bank accommodation has been much higher in the US**



Source: Bloomberg, data as of 04 March 2021.

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In our [equity strategy for this year](#), we advocated how China warrants consideration

within a strategic asset allocation. The implication of renminbi's strength is, therefore, not only important for currency investors but crucial for investors of all asset classes in deciding whether to consider hedged or unhedged exposures.

**Source**

<sup>1</sup> WisdomTree , Bloomberg. From 27th May 2020 to 4th March 2021.

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