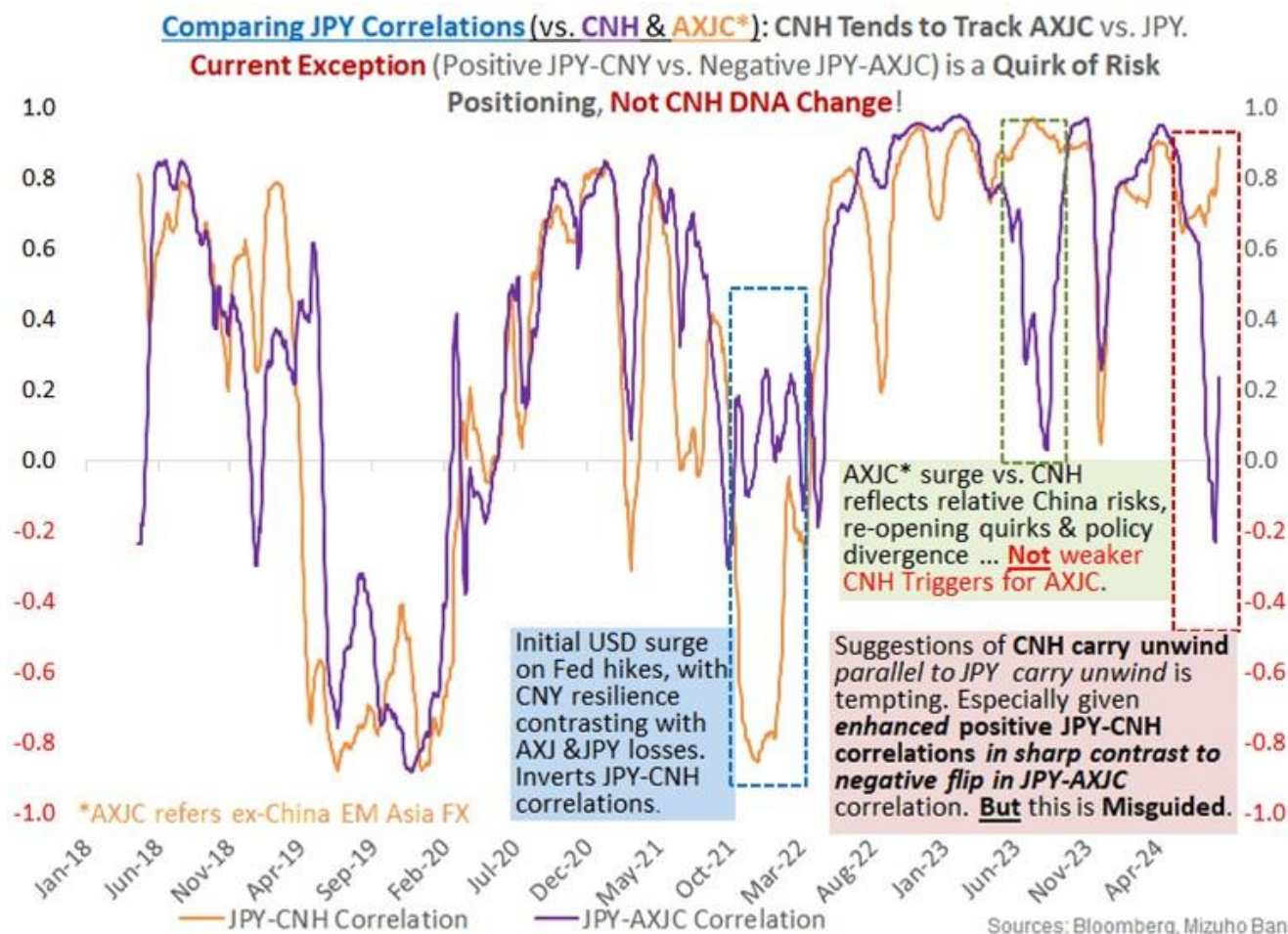
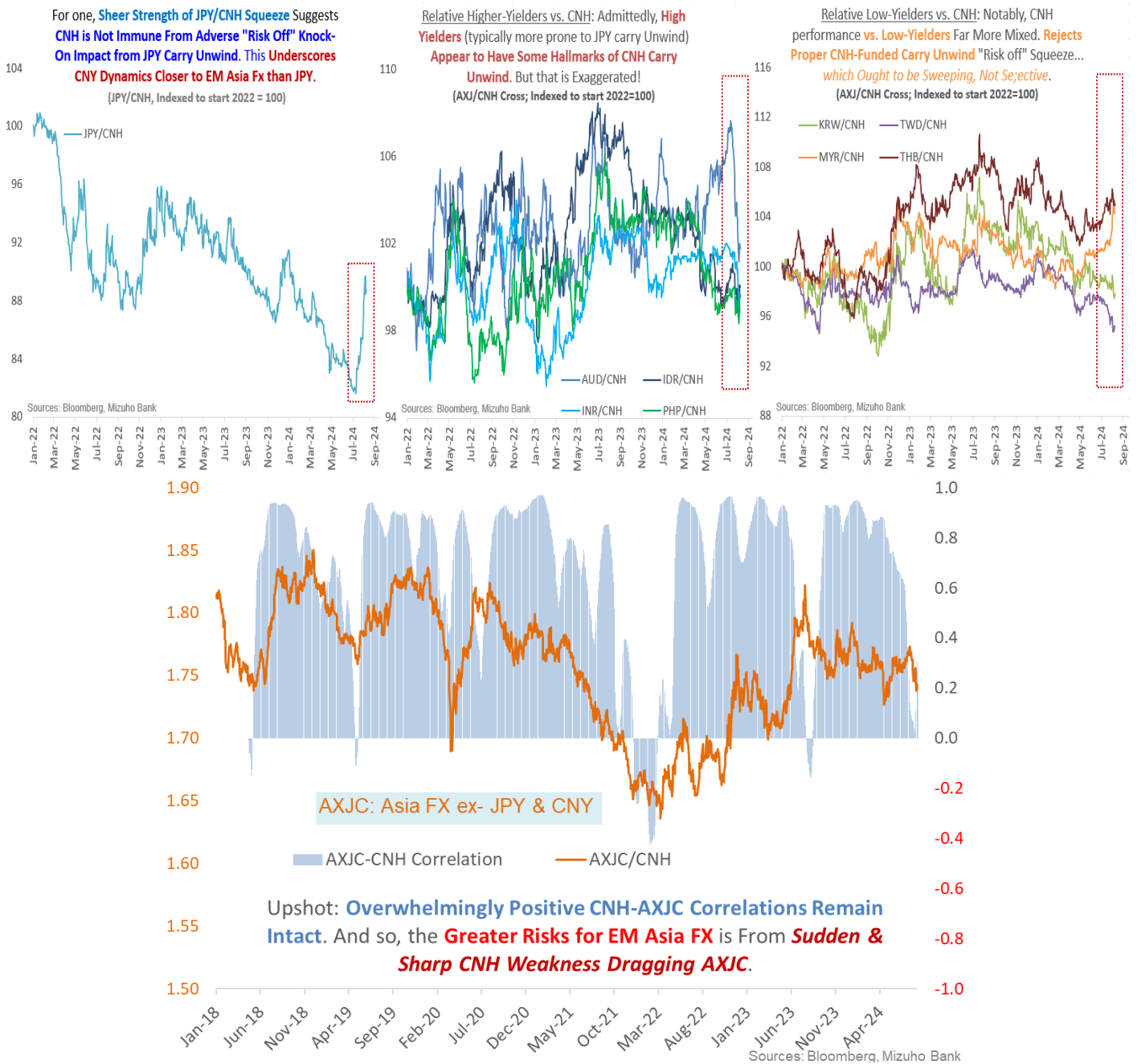


Why CNY Carry Unwind is Not the Next Big Shoe



- It is understandable why **CNY carry unwind** is now being targeted as **the next proverbial shoe to watch**.
- Especially *given distinctly positive correlation between JPY and CNY* over these tumultuous JPY carry unwind sessions.
- But this is a **somewhat misguided** view as the **imagined and exaggerated parallels between the CNY and JPY don't all stand up to scrutiny**.
- Most obviously, **JPY is a deeply liquid, global currency**. The **CNY is significantly less so** given capital controls and PBoC guidance/implied bands.
- Second, the **BoJ may be normalizing**. *But in sharp contrast, the PBoC needs further loosening* to escape deflation.
- In turn, **unlike JPY bulls liable to be agitated into action by Fed cuts** (given implied Fed-BoJ divergence) **CNY may be subdued** given less emphatic Fed-PBOC divergence.
- Third, **CNY weakness goes well beyond the rates (differential) story**. Instead, it is **predominantly driven by structural economic headwinds and daunting geo-political threats**.

- So, for **CNY squeeze triggered carry unwind to endure and be emphatic, the pre-existing (and overwhelming) geo-economic risks to fade as well.**
- Admittedly, **during an episode of pronounced JPY carry unwind**, sympathetic, knee-jerk **CNY carry unwind is not a negligible risk.**
- **But** this is unlikely to be the persistent and profound threat for EM Asia FX. Rather, **adverse CNY depreciation may be a far bigger risk as sympathetic EM Asia FX drag kicks in.**
- Simply put, in our view, the **biggest shoe that can drop is one of CNY meltdown that cascades down as wider "risk off"** and **not CNY-funded carry unwind per se.**
- In other words, **while excessive volatility either way is not desirable, we fear abrupt CNY meltdown more than we do sudden CNY strength.**



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