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Citi Wealth

Asia Pacific
Regional Publication

Jaideep Tiwari
Head, Global Foreign Exchange Investment Strategy

22 May, 2025

FX Focus: USDCNY – Trade Truce and Implications For RMB

FIGURE 1: FX Forecasts

Forecast (Apr 2025)	Spot	0-3m	6-12m	Long-term
USDCNY	7.2070	7.4000	7.3000	6.9000

Source: Citi Wealth Investments as of Apr 2025.

The US-China tariff reductions announced on May 12th in which both agree to cut tariffs for 90 days until August 10th (vs July 8th for the rest of the world) are significantly bigger than expected. The US agrees to lower tariffs to 30% from 145% and China to 10% from 125%. The new tariffs will lower the effective tariff rate on China to between 38 - 45%, taking the US – China trade relationship back to non-prohibitive days.

The two agree to:

1. Cancel the tit-for-tat escalatory tariffs of 91% since ‘Liberation Day’ on April 2nd.
2. Suspend 24% of the reciprocal tariff on China in 90 days while keeping the 10% baseline reciprocal in place. China also suspends curbs on exports of rare earths and other goods and technologies for 28 US entities (Bloomberg).

Looking ahead, the 20% Fentanyl tariff could be a low-hanging fruit for further reduction and its rollback could remove another external hurdle for the Chinese economy.

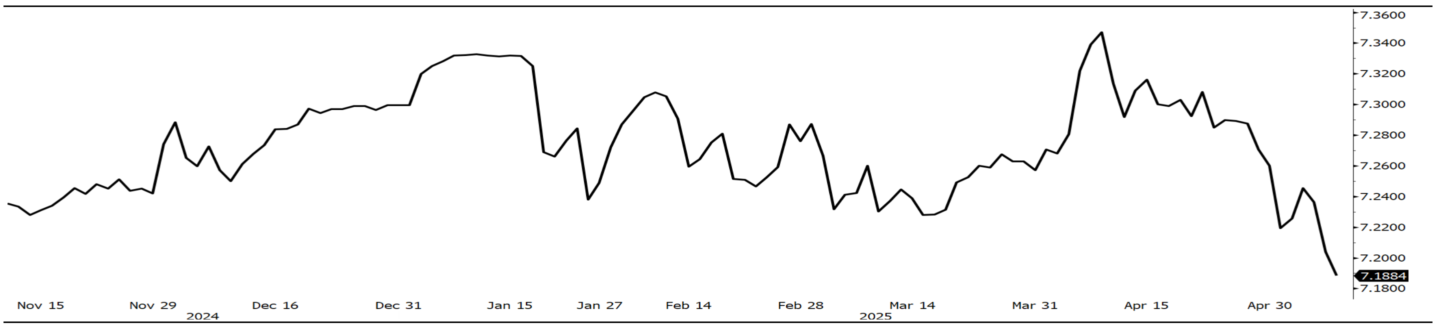
The reductions will significantly narrow tariff rate differentials between China and other trade partners, leaving Chinese exporters with more wiggle room. But the downside to this is that with trade tensions significantly defused for now, the urgency for fiscal and monetary stimulus in China may be lower as the economic impact on China’s GDP growth is smaller than previous estimates. However, none of this is a done deal and uncertainty remains, noting the currency has not even been discussed, a known issue for President Trump.

China’ strategy since early 2025 has been to keep USDCNY spot relatively stable to avoid triggering a self-reinforcing cycle of devaluation expectations and capital outflows (akin to 2015/2018/2022-23). However, China has allowed CNY to decline against the trade-weighted CFET basket, reflecting its willingness to weaken the currency against non-US trading partners. The strategy seems consistent with China’s diversification of trade flows away from US to Asia (East and South-East Asia now rank as China’s top trading partner).

In theory, the new US effective tariff on China at a still elevated 38 – 45% should give PBoC the incentive to allow CNY to weaken. Instead, the rapid pace of tariff de-escalation is leading to speculation about a possible currency accord between US and China to strengthen CNY. However, a weaker exchange rate would run the risk of China being labelled a currency manipulator by the US Treasury. More likely, markets expect China may allow the RMB to strengthen as a quid pro quo to any formal US – China trade deal.

But the pace at which CNY appreciates would need to be gradual to mitigate financial stability risks within Asia EM that could emerge if USD drops too quickly or in a disorderly way as Asia EM economies hold a large amount of USD denominated investments. Ultimately, potential CNY gains could be significant under a currency accord, but the pace and timeline related to any strengthening in CNY will need to be determined by China.

FIGURE 2: Over the past 6 months USDCNY has traded in a 7.200 – 35 range



Source: Bloomberg, May 13, 2025.

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