13 February 2013

HSBC Global Research

Currency War Special

Battle cries, FX thrives

The currency war is intensifying: the number of participants is rising, fresh policy tools are being used to fight, and the scale of influence on the wider FX market is increasing.

We examine 36 currencies and demonstrate that there has been an increase in currency war appetite over the last year. We grade each country based on a scale of 0 to 10, with the highest score for those we believe are most open to the idea of acting in currency markets, one of the drivers of which may be to secure an economic advantage. The average score has risen over the last year. We also determine whether such activism could be justified on the basis of FX valuations, comparing currency war appetite against their relative under or overvaluation.

Countries that have become more activist include Japan and Switzerland in G10, and a number of countries in LatAm. EMEA has been relatively less embroiled, though the CZK and TRY feature. Interestingly, our score for Asia ex-Japan has declined as central bank intervention is increasingly targeted at lowering volatility rather than seeking a more competitive exchange rate. However, scores in this region remain high given their past appetite for intervention. The fear for the market will be that any additional JPY weakness might stir central banks to be more active, ratcheting up the currency war.

There are a number of investment implications:

1 Those currencies not actively participating in the war will likely see further upside should the conflict worsen. This grouping includes the EUR and G10 commodity currencies.

2 The JPY now appears undervalued, and Japan is likely to face sterner international opposition, limiting further depreciation of the JPY.

3 The data matters once again, either strengthening or undermining the case for currency war. If the global economic recovery stalls once again, the scramble to secure a share of a limited economic prize will make the currency war even more bitter. By contrast, a stronger global upswing would see such FX tensions fade.

4 The currency war phenomenon means FX will lead other asset classes, rather than following them. FX is back in the driving seat.

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Market focus

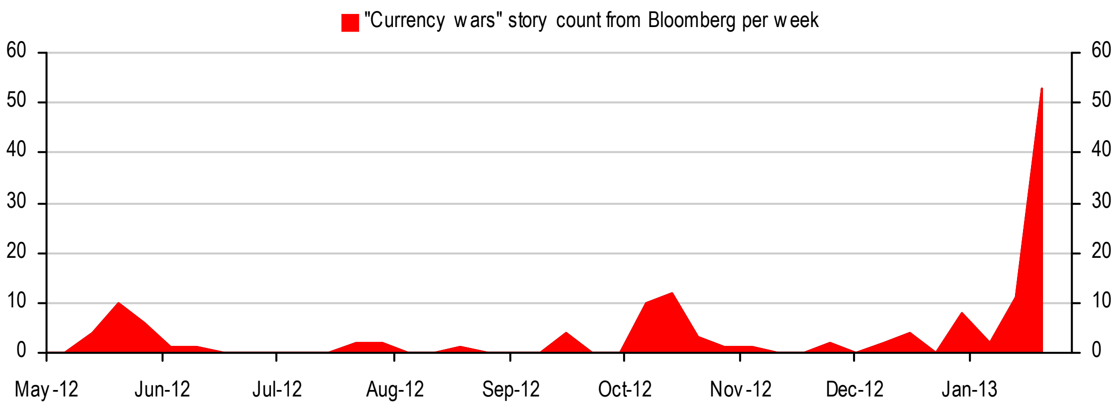
Mobilising forces

"History teaches that war begins when governments believe the price of aggression is cheap."

Ronald Reagan

We are in a currency war. Japan's efforts to weaken its currency have been a high profile development in this war, but far from first or the only one. Many nations have been cutting rates and embarking on non-conventional easing to help revive activity, and currency weakness was always a likely side-effect, whether intended or not, of such action. Switzerland introduced its floor on EUR-CHF back in September 2011. Intervention to limit currency strength or target currency weakness has long been in the tool-kit of some emerging markets, but in many instances, the frequency and breath of action is on the increase. One other thing is clear – currency wars are becoming a bigger talking point. Chart 1 shows the number of times the phrase "currency war" has been mentioned on Bloomberg. As the internet generation would say, currency wars are trending.

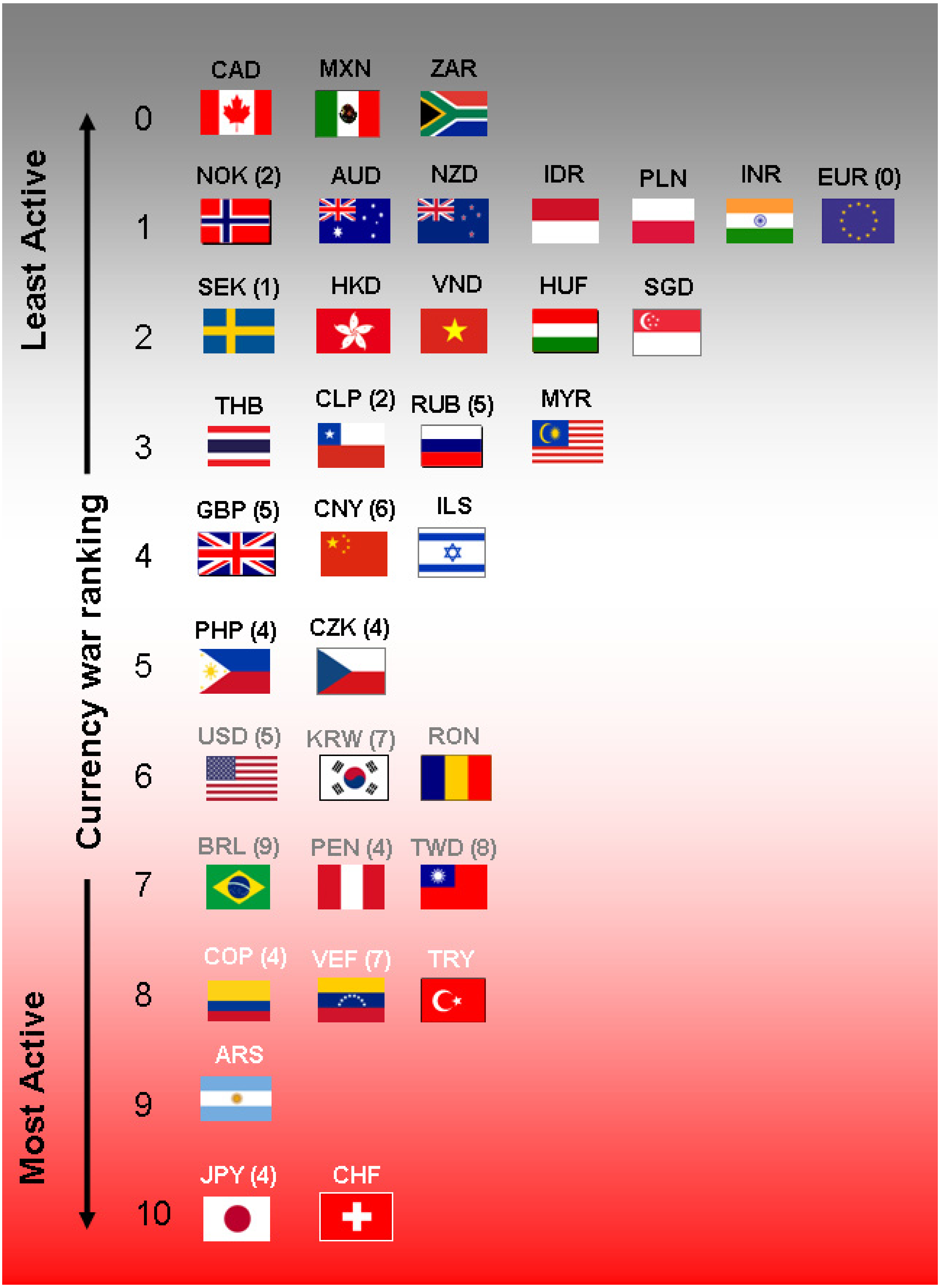
1. Currency wars are trending.



Source: Bloomberg, HSBC

Not everyone subscribes to the currency war theme. For example, the IMF's chief economist believes talk of a global currency war is "overblown" while Bank of Canada's governor said there is "no sign of a currency war globally". The previous governor of the SNB argues that currency weakness is often just a side-effect of central banks seeking to meet their policy mandates. One could have some sympathy for their view. After all, manipulation of currencies by policymakers is hardly a new phenomenon, be it in emerging markets or G10, and currency weakness may simply be a side-effect of the new era of zero interest rates and unconventional easing.

2. Where do currencies lie on the "currency war" spectrum?



Source: HSBC, Wiki commons Note: Figures in brackets are for Jan 2012

A weak global economy makes the same behaviour feel like war

Yet others, such as the head of the BIS, point to the pressure central banks are under from government to stimulate growth, including having a weaker currency. German Chancellor Merkel noted that she was "not without some concern about Japan right now". French President Hollande has been vocal about the impact of a strong EUR on competitiveness. Why does it feel like a war when much of what we are seeing is not new?

The answer is likely the state of the world economy. Previous FX manipulation sought to retain or build a share of a growing global economy. The pain of your neighbour stealing some of your market share through currency manipulation was offset by the happy realisation that your situation was still improving. Your share of the pie was smaller, but the pie was so much bigger, it did not matter. Now, the pie is not growing, and the pain of dwindling market share is much more apparent. So the same behaviour feels more like war.

Our analysis suggests that examples of behaviour consistent with currency war are on the rise. Chart 2 on the previous page shows our score for 36 currencies based on their appetite for conducting a currency war. The scoring is, by nature, rather subjective and many will have different views. In reaching our scores, we take account of whether policymakers are using tactics such as rhetoric, interest rates, direct intervention, quantitative easing or regulations to try and influence their currency.

Those with a low score are the least open to the idea of acting in currency markets to secure an economic advantage. This grouping includes the free floating currencies of G10, but also a number of emerging market currencies as well.

Pegs may be active in the FX market, but they are not at war

It is worth noting that we have given many pegged currencies a low score. Although they may at times be active in the currency market to protect their peg, many of which pre-date the recent escalation in conflict. We are trying to identify the appetite for a currency war. So HKD, RUB and arguably the SGD with its long-running NEER policy are not at war. The VND fixing rate has been unchanged since late 2011, suggesting that, for the time being at least, we can essentially treat it as another peg.

JPY and CHF are at the front line

At the more active end of the scale lie the JPY and CHF. Some might argue that the CHF is a pegged currency and is akin to the HKD, for example. But the Swiss floor was introduced with the express purpose of preventing additional CHF strength. It is the classic example of a currency war weapon. The CHF scores a 10. So too the JPY given the active efforts to weaken it through rhetoric, a higher inflation target, promises of future monetary easing and a government adamant that it can bring inflation back.

Battle tactics are evident to varying extents across emerging markets

The highest score among emerging markets is Argentina, where the central bank intervenes regularly to weaken the nominal exchange rate to maintain FX competitiveness, rather than simply acting to limit currency strength. The middle ground of our scale is replete with currencies where policymakers seek to influence currency behaviour, the score reflecting the extent of their zealousness.

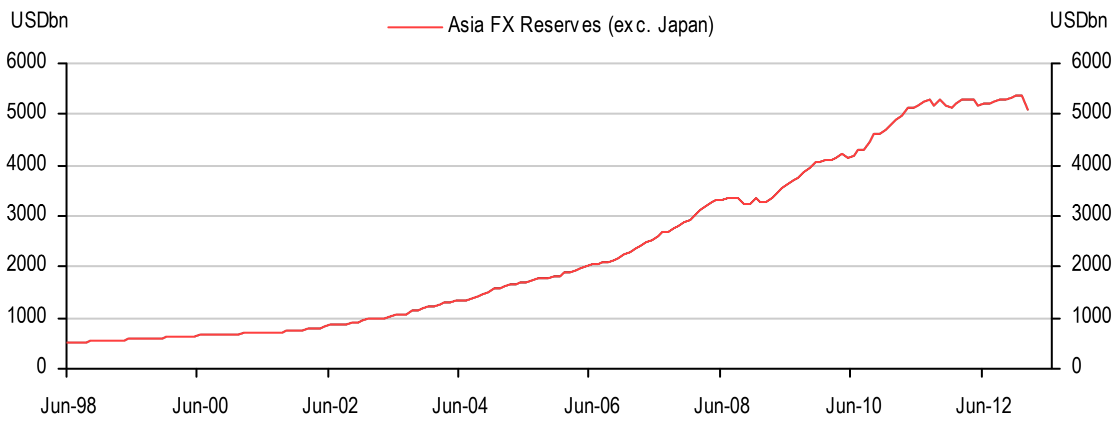
But what we are really interested in here is how the currency war threat is developing. Chart 2 also shows the scores for the previous year in brackets for any currency that has seen a shift over those twelve months. For example, a year ago, the JPY would have scored a "4" rather than its current "10".

The average currency appetite score is rising

This approach shows that the majority of moves have been towards higher scores. There has been a notable hardening of attitudes in LatAm with the CLP, COP and PEN all moving higher on our scale. The process continues with Peru recently announcing it will pay back foreign debt early this year, Colombia cutting interest rates and an intensification of intervention. Venezuela has just devalued its currency, although this may have more to do with fiscal than export considerations. Most of the scores within EMEA are comparatively low and stable, with the notable exception of the TRY. Japan represents the main mover in G10, and the shift would have been even more marked were we to go back to 2011, before the Swiss introduced their floor.

Interestingly, the scores in Asia ex-Japan are lower now than in 2012. Intervention in currency markets has long been a favoured tactic in this region, and is reflected in the scores which are high by global standards. However, the mindset has moved away from a one-side limiting of appreciation towards a two-sided limiting of volatility (see *'KRW: talking tougher'*, Asian FX, 22 November 2012). Furthermore, the scale of inflows into the region is less marked than previously, reducing the need for activism from central banks. Scores for KRW and TWD are both lower in 2013. A chart of Asian FX reserves excluding Japan (chart 3) shows that the accumulation of reserves has flattened over the last year, likely due in part to the less activist stance of FX policy in the region.

3. Asian FX reserves are no longer being built up



Source: Bloomberg, HSBC

But the main headwinds to an even higher currency war score came from Russia and China who both saw their scores fall. In Russia, the CBR maintains an exchange rate target, but it is being liberalised with a target of a free floating currency by 2015. In China, the PBOC has become increasingly 'hands off', and the FX regime is becoming more market driven and liberalised. Our China economist believes the CNY will be fully convertible within five years (see *'A convertible RMB within five years'*, Currency Outlook November 2012). So while some of the world is engaged in a currency war, Russia and China are pushing in the opposite direction.

Developing weapons of mass depreciation

The tactics of a currency war used to be relatively straightforward. The traditional weapons of currency intervention have been:

1) Rhetoric.

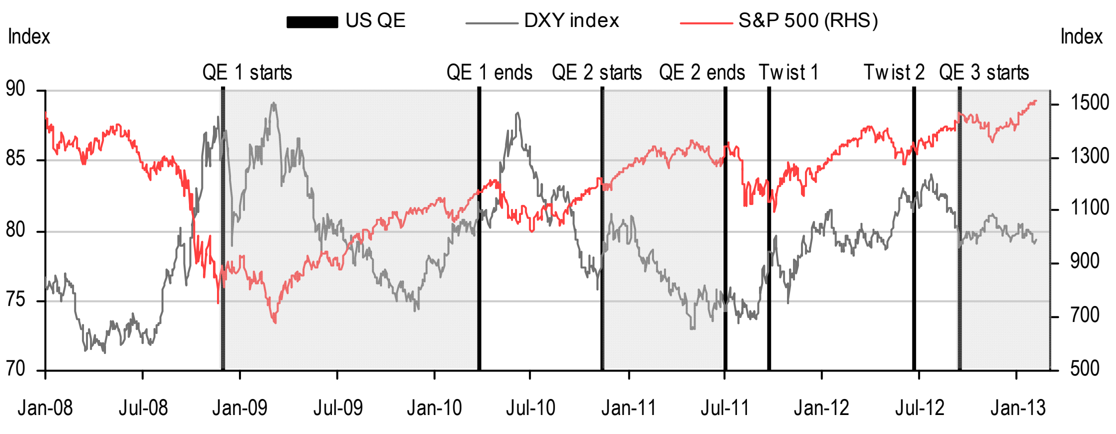
2) Rates.

3) Direct intervention.

Central banks or governments express concerns over a currency's high value, lower interest rates to diminish its yield appeal, or sell their currency directly to the FX market to lower its value. In many instances, these tools are still used. For example, Japan has been actively talking its currency lower, the Czech central bank too. Turkey has used its myriad of policy interest rates to reduce the TRY's appeal, while some Asian central banks continue to intervene in the market, albeit in a less active way than in 2012.

However, a new era also demands new weapons. For much of G10, the interest rate channel has been exhausted with nominal rates close to zero, the direct intervention channel unpopular for international political reasons, and rhetoric impotent as a consequence. Quantitative easing, in its many shapes and forms, may not actively target currency weakness but in many instances it is a likely or even desired side-effect. For example, Spencer Dale, Chief Economist of the Bank of England, noted that a weaker currency can be a side-effect of QE as the proceeds of central bank asset purchases are moved abroad by foreigners, providing an economic benefit. In our currency war appetite measure, the USD has moved higher because the US Federal Reserve has opted for open-ended QE. By contrast, the GBP measure has moved lower because the Bank of England has not added to its QE pool since mid-2012.

4. US QE has contributed to USD weakness



Source: Bloomberg, HSBC

In emerging markets, regulations have become a favoured additional tactic, for example changes to tax laws or new macro prudential measures where currency weakness is a likely result. Brazil is one notable example of this, where new taxes were levied on financial transactions that were pressuring the BRL. Others have increased reserve requirements on foreign purchases of local assets, or sought to increase incentives for domestic investors to channel money abroad.

Justifying conflict

Thus we are in a currency war that is broadening not only in terms of the number and intensity of its protagonists but also in the tools being used to fight it. Yet, as is so often the case in conflict, those participating believe their actions are justified. The logic can vary. Sometimes the fight is against speculation, sometimes against destabilising volatility. Others point to a grossly overvalued currency as warranting remedial action, others to the currency as a sole means of stimulus when all alternative options have been exhausted. Another excuse likely to gather prominence is that aggression is warranted simply as a defensive response to the aggression of others. For currency markets, this race to the bottom could be the equivalent of mutually assured destruction.

We judge the justification for war on the basis of valuation. Countries with a highly over-valued currency can lay a greater claim to justified intervention than those with an undervalued currency. There are many approaches to determine a currency's fair value. We choose three:

1) **Current Real Effective Exchange Rate (REER) compared to its 5-year average.**

2) **OECD measure of purchasing power parity.**

3) **The Big Mac Index**.

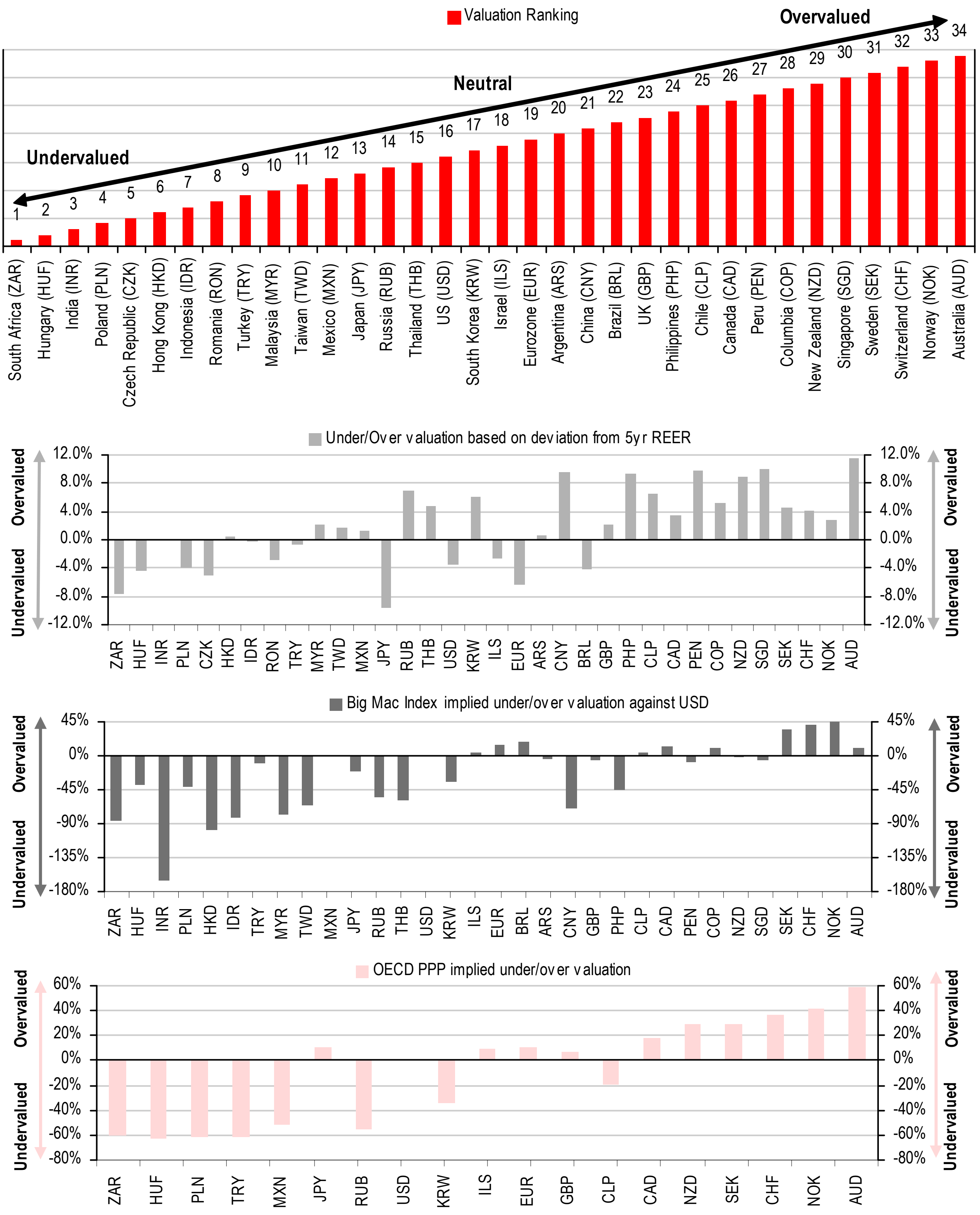
We rank the currencies in order based on each of these measures, and then calculate their average rankings[1]. The results are shown in chart 5. For example, on this approach, AUD is the most over-valued currency currently; the ZAR is the most undervalued. We would emphasise this is not a buy/sell indicator, rather a way of gauging if there might be justification for war.

The charts on the next page combine this valuation ranking with our earlier assessment of a country's appetite for engaging in currency war.

- The valuation rankings are shown on the x-axis, the most undervalued currencies towards the left hand side, the "richer" currencies towards the right.
- Currency war appetite is shown on the y-axis, the least active towards the bottom, the most active towards the top.

[1] *OECD PPP measures are not available for some emerging market economies. In these instances, we use their average ranking for the REER measure and the Big Mac Index.*

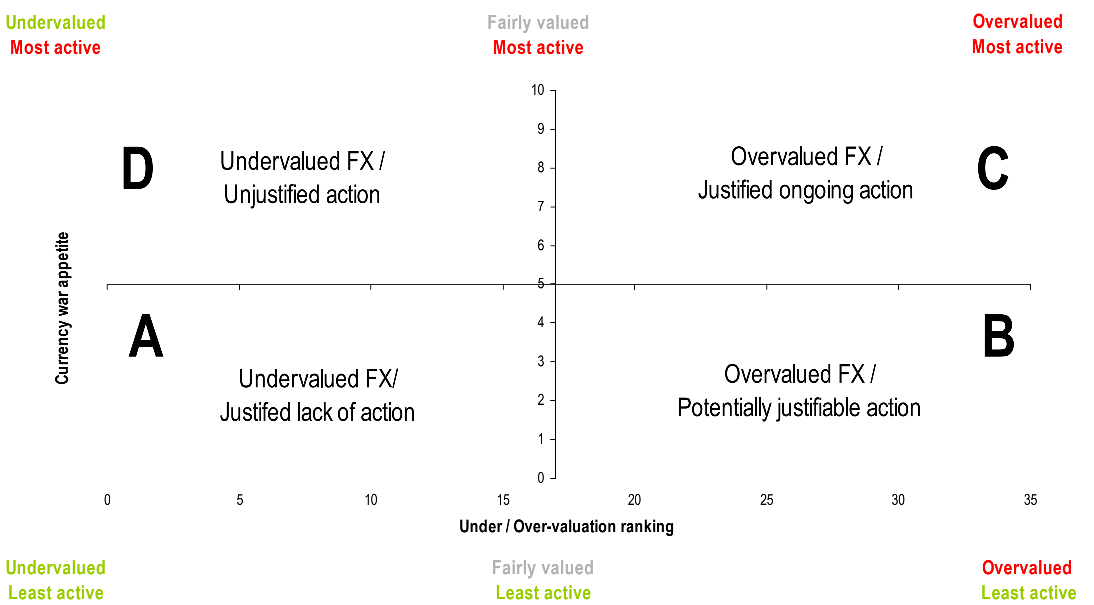
5. Currency valuation ranking based on PPP, Big Mac Index and REER levels



Source: Bloomberg, OECD, HSBC

This creates four broad quadrants, shown in Chart 6. We then populate these four quadrants with the results of our currency war appetite index and our valuation measures (charts 6 & 7).

6. Combination of currency valuations and currency war appetite



Source: Bloomberg, OECD, Wikicommons, HSBC

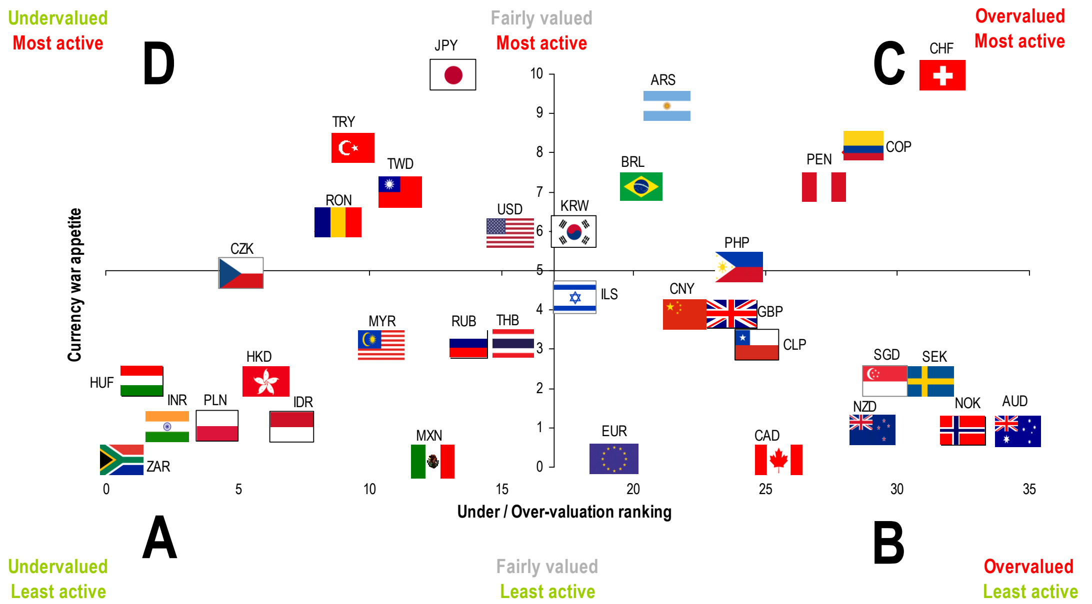
A. **Undervalued / Least active**: These currencies are not active in the currency war, but their undervalued nature suggests there is little reason for them to join the fight. The grouping includes a number of EMEA currencies, including the ZAR, HUF, and PLN. These should be able to contend with efforts elsewhere to weaken currencies as their starting point is relatively competitive. In essence, these are the currencies you would want to buy if you believed the currency war were to intensify further.

B **Overvalued / Least active**: The G10 commodity currencies feature prominently in this segment of currencies where policymakers are not seeking to weaken their currencies or actively curtail their strength. Arguably, they could justify such action given their overvaluation but for now most have restrained themselves to mild rhetoric or, in some instances, modest rate cuts. Should the war intensify, these currencies may prove to be the mirror of targeted weakness elsewhere. We believe the EUR could be especially prone to gains, a view we discuss in more detail later.

C **Overvalued / Most active**: The top right segment are those currencies which are fighting currency strength but have either been unsuccessful or have more work to do. Their comparatively overvalued nature means they can argue some justification for their more activist stance.

D **Undervalued / Most active**: potentially the most contentious segment as policymakers continue to act against currency strength or actively seek to engineer currency weakness even though their currencies do not appear overvalued. The JPY is in this category, as is the TWD although its intervention increasingly seeks to reduce volatility rather than target direction and it also has a lower score than last year. Turkey, with its love of interest rate adjustments, also features.

7. A snapshot of currency war appetite and FX valuation

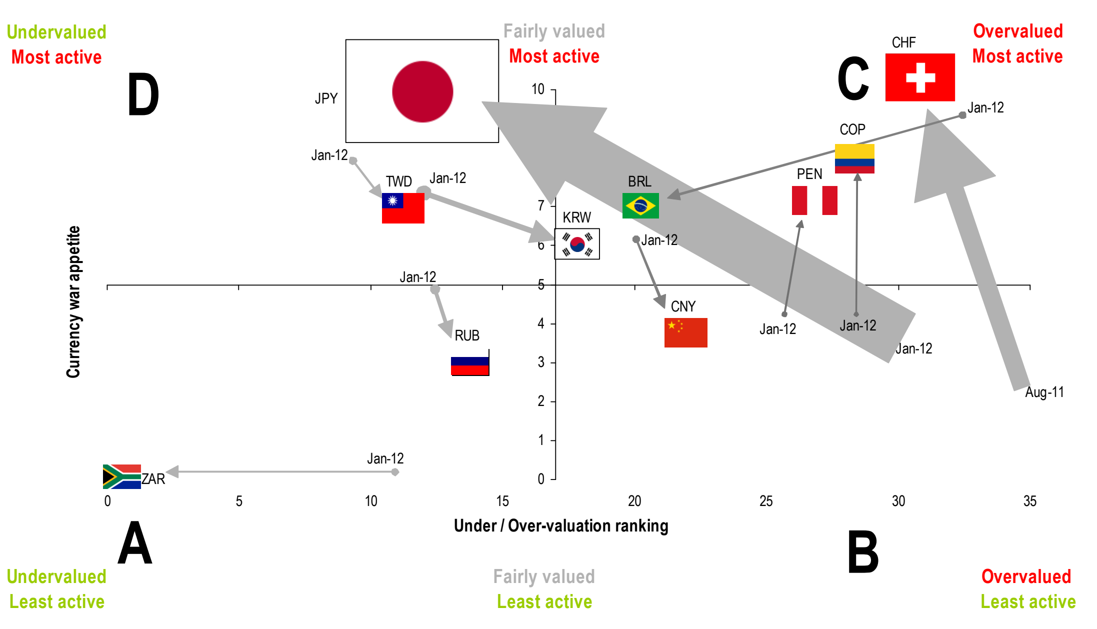


Source: Bloomberg, OECD, Wikicommons, HSBC

The approach is further illuminating if we consider the big changes using these parameters, illustrated in chart 8 below. The RUB and CNY see their scores lower, reflecting their push towards more liberalised currencies. The TWD and KRW also have lower readings, as they seek to lower the volatility rather than the value of their currencies. The BRL has also become less combative over the last year, a stance consistent with its less overvalued currency – a measure perhaps of the success of its earlier interventionist ways.

However, these are the exceptions. The ratings have moved higher for a number of LatAm countries. The CHF moved from the overvalued and least active segment ahead of the introduction of the EUR-CHF floor to its current position among the most activist. However, it suggests some justification for its initial intervention. The JPY was in a similar position a year ago, but the sharp weakening of the JPY since then has undermined the case for further targeted currency weakness by Japanese policymakers. Japan's government seeks to characterise the sliding JPY as a correction from an overvalued level, and our chart lends credence to this view.

8. Key movers in the currency war (thickness of arrows show relative size of FX market turnover)

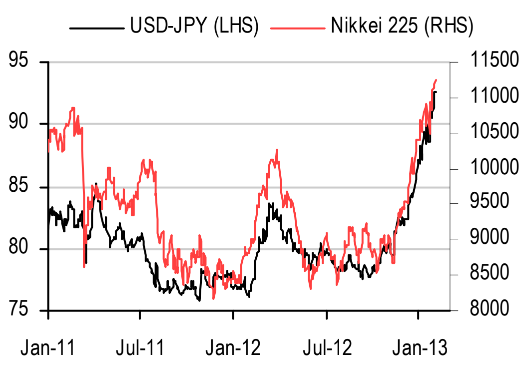


Source: Bloomberg, OECD, Wikicommons, HSBC

Combatants rise in number and influence

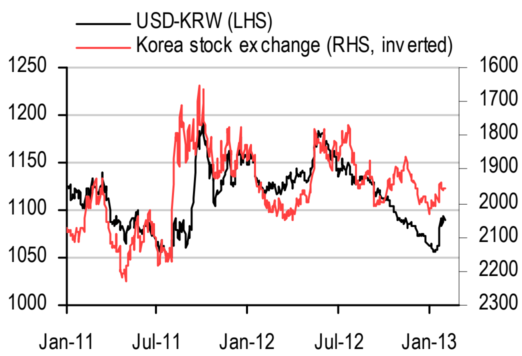
Yet it also suggests this argument is now out of date. In addition, the entrance of the JPY to the currency war is a very different beast from other currencies. FX spot turnover in the JPY is USD300bn a day, three times bigger than the CHF, which itself is 11 times bigger than the BRL. We have illustrated the relative scale of these currencies by the size of the arrows in Chart 8. The global market may have been able to contend with an interventionist CHF administration, but the scale is different when the JPY becomes embroiled in the battle. So not only is the number of combatants on the rise, but also their sheer scale of influence on the FX market.

9. Japanese equities capitalise on JPY weakness



Source: HSBC, Bloomberg

10. Stronger KRW a headwind



Source: HSBC, Bloomberg

February 14 G20 meeting

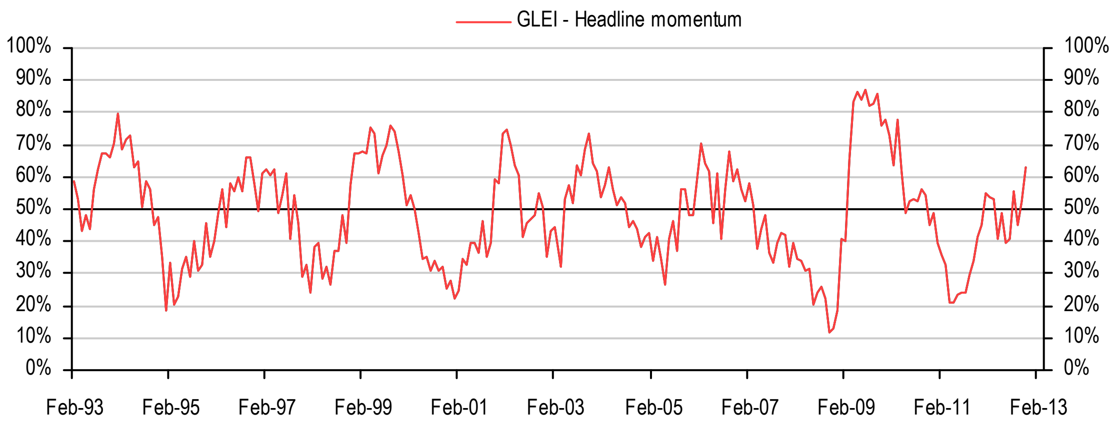
At G20 meetings, there will only be four currencies represented who appear more undervalued than the JPY on our metrics. The impact is already being felt. The JPY has become more of a regional FX focus having gone largely un-noticed for many years. Suddenly, Asia-ex-Japan may have to spend a lot more energy considering their position relative to the JPY. For example, Japanese equities may be capitalising on the weaker JPY (chart 9). Korean equities are clearly not (chart 10).

Where next for the war?

Sayre's law states that "in any dispute, the intensity of feeling is inversely proportional to the value of the issues at stake." This applies in a currency war, where the smaller the value of the global economy, the greater the likely fight to secure a share. There are some grounds to assume that things are improving. Data on China is accelerating, defying those earlier fears of a hard landing. The US economy is showing some signs of life, and the labour market is slowly improving. In Europe, PMIs are inching higher. HSBC's proprietary global leading indicators, a collection of 120 signals, are showing upward momentum (see chart 11). If the upward trajectory can be sustained, the pressure for policymakers to seek a weaker currency will diminish. If the pie is getting bigger, the fight to get a slice will be less gruesome. In a world of deficient domestic demand, one devalues to gain growth, but with a smaller pie to share, this market share grab is more clearly at the expense of others.

The problem is that we have been here before, where hopes of an economic upswing have come unstuck over time. The current danger is that the market is mistaking a reduction in tail risk (e.g EUR break-up, US fiscal cliff and China hard landing) for a genuine improvement in economic fundamentals back towards the pre-crisis norm (see *'FX – why data now matters'*, Currency Weekly, 1 February 2013). Thus the gains in risk appetite could come undone unless the data gains can be sustained. Until the outlook becomes clearer, the appetite for currencies to be used as a tool of economic stimulus is likely to enjoy support in certain countries, particularly in those which do not face price pressures, be it in terms of consumer price inflation or asset price inflation.

11. Global leading indicators are showing signs of upward momentum



Source: HSBC, Bloomberg

Another factor to consider in the evolution of the war is tolerance for other's actions. So far, Japan's tactics that have weakened the JPY have not provoked a stern rebuke. The recent G7 communiqué merely repeated calls for a market-determined exchange rate. Asian central banks have not been particularly active in the market to act against their currencies' rise against the JPY. However, were JPY weakness to persist or intensify, the market will fear that this patience might run out.

Activism is not cost-free

A further consideration in the likely evolution of the war is to consider the costs of conflict or the constraints on activism. We noted in the context of Japan that the reaction of the international community to currency interventionism would be one constraint. But some countries might not view this as a problem.

Another point to remember is that intervention has costs. For example, a weaker currency can lead to higher inflation. Brazil has used its currency to stimulate growth, but has recently acknowledged the adverse impact this is having on inflation. The future extent of BRL weakness is likely to be more muted as a result. Switzerland's direct intervention has seen their foreign exchange reserves balloon, and any leakages from this intervention into the local economy risks inflating local asset price further. Norway's rate cuts to stem the NOK came to an end, in part because of the knock-on effects on the already buoyant housing market. Sterilisation can help, but here too, interest rate differences means intervention is not a costless exercise.

Investment implications

There are a number of investment implications of this ongoing intensification of the currency war.

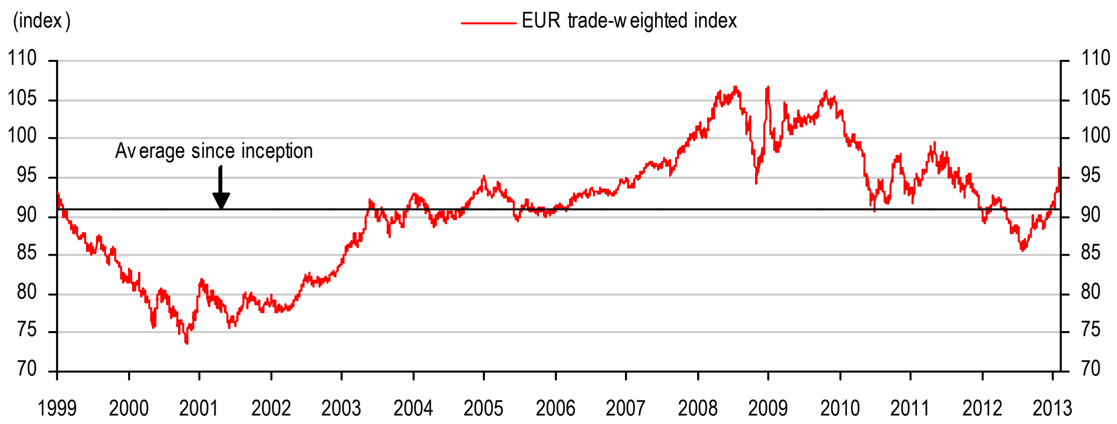
1) Less activist currencies, notably the EUR, may be the 'safety valve' for depreciations elsewhere.
2) The JPY sell-off is likely to face sterner international opposition, limiting further moves.
3) The data matters once again, either strengthening or undermining the case for currency war.
4) FX is regaining its prominence, often acting as a leader of other asset classes.

The price of less active intervention

Currencies are a relative game, and for those countries targeting a weaker currency, there is always going to be a flipside stronger currency. In some instances, this will lead to countries having to cope with overvalued currencies. We identified these above as the Scandies and G10 commodity currencies. To some extent, they are trying to lean against the wind to limit the damage. Australia and New Zealand continue to highlight the overvalued level of their currencies, a reality which has contributed to lower interest rates in the past and will likely hinder the extent of rate hikes in the years ahead. Norway and Sweden have also used lower interest rates to curtail currency strength in the past, although high domestic credit growth and housing bubbles limit this as a tool going forward.

However, the standout currency may in fact be the EUR. It may not be as overvalued as some others in the less active category, but it is heading in that direction. The ECB acknowledged at its latest meeting that the EUR forms a part of the interest rate debate insofar as it has an impact on inflation projections. It prompted us to give the EUR a score of "1" rather than "0" on our scale. Draghi was, however, also keen to note that the EUR is broadly trading in line with long-term averages (see chart 12). In fact, worrying about too strong a currency may feel like a luxury to the ECB having spent a couple of years merely trying to ensure its survival.

12. EUR is not stretched by historical standards



Source: Bloomberg, HSBC

Further EUR strength could see the ECB's attitude harden. In November 2004, ECB president Trichet said the currency's rally was "not welcome" and described the market moves as "brutal". EUR-USD was trading at 1.30 at the time. This trimmed some of the enthusiasm for the EUR, but the exchange rate eventually moved to 1.60. Today, similar expressions of concern by the ECB could have a similarly limited impact unless the market believed the ECB would get aggressive to counter EUR strength. It would have to believe the ECB was about to join the currency war in earnest. This feels unlikely for now.

After all, what could they actually do? With interest rates so low, any concerted effort to prevent EUR strength would likely need to include some form of quantitative easing once the remaining interest rate ammunition was exhausted. Some might argue that a triggering of the Outright Monetary Transactions (OMT) would be equivalent to QE, but given the ECB's promise of full sterilisation of OMT, this is not the case. Genuine QE, involving the unsterilized purchases of government bonds of every country in the Eurozone by the ECB, feels a very distant prospect at present. EUR strength remains one likely 'safety valve' for any intensification of the currency war, ie as an offset to depreciation efforts elsewhere.

JPY activism to face international headwinds

Japanese authorities argue that the current weakness of the JPY is a correction from an overvalued level. This may be true, but it is a more difficult argument to defend from this point forward given the 20% drop already seen in the trade-weighted JPY. Within the Asian region, the KRW has appreciated by 30% against the JPY since May 2012. We continue to believe that, ultimately, failure by Japan's authorities to deliver on the radical promises of reflation will see the JPY retrace much of its recent weakness. However, in the meantime, international political opposition to further engineered JPY depreciation is likely to intensify. It will be a further headwind to an extension higher in USD-JPY.

The other consideration regarding Japan will be how successful the policy proves. If Japan's economy responds quickly to the stimulus of a weaker currency and the boost to local asset values it delivers, then others will be more tempted to follow suit. Ironically, therefore, the more successful the approach, the greater the number of those likely to mimic it, which in the end makes it more likely all those playing the game will end back at square one.

Data matters

We have noted recently that data is regaining its traction in the FX market as investors try to divine whether the global economy is heading for sustainable recovery. As noted above, the data will also determine the intensity of the drift towards currency war. As a result, the currency war debate is helping to drive the FX market away from simple considerations of risk-on risk-off, and back towards the more traditional approach where currency prospects were shaped by the data, both international and local. The danger for currency markets is that any fresh deterioration in the global data would therefore increase the risk of "beggar thy neighbour" FX policies, which could in turn further undermine confidence.

FX matters

The resurrection of the currency wars theme has revived the prominence of FX as an appropriate asset class to express a view. During the height of the RORO phenomenon and the death of the carry model, FX lost its allure as currencies struggled to work out what the FX implications of non-conventional easing were for a given currency. QE in the US was USD negative, in the Eurozone LTROs were ultimately EUR positive, and in the UK QE was GBP neutral. The implications of QE for bonds and equities were far more straightforward.

In this currency war environment, FX becomes the obvious way to express a given view. If you believe the Japanese will successfully engineer ongoing FX weakness, you express it through the JPY. The equity market may rise due to JPY weakness, but it will be in response to the FX market. Equities will not lead the way. Japanese bond markets will face the ambiguity of additional buying from the Bank of Japan against the threat that the reflation policy might ultimately prove too successful with attendant problems for bond prices. If currencies are heading for conflict, FX will of course be the front line.

Conclusion

The currency war is here. The number seeking advantage through their currency is on the rise, and with Japan now active, so too is the scale of these combatants' influence on the wider FX market. How bitter the battle becomes will depend on how swiftly the global economy can recover. Any setbacks will likely increase the appeal of currency-induced stimulus. Invariably there would be winners and losers in any such battle. Further JPY weakness will face greater international political opposition. Less activist currencies notably, but not exclusively, in G10 will see additional upside should the war get worse. But it is an issue which puts FX at the forefront of global financial markets, a leader of sentiment in other markets rather than a follower.

Appendix A: Currency war appetite

	Currency war appetite		Description of attitude towards FX and tools (if any) being used to target FX
	Jan 2012 score	Jan 2013 score	
G10			
US (USD)	5	6	Policymakers' not explicitly targeting a weaker USD, but this is one widely expected side-effect of ongoing QE. Hard to say how much weaker this has made USD as we do not have counterfactual evidence.
Eurozone (EUR)	0	1	ECB avoids talking about FX other than to repeat G20 view that FX should be determined by market. More recently, some politicians have begun to express concern about EUR strength and currency weakness elsewhere.
Japan (JPY)	4	10	Actively talking down JPY and advocating radical easing of monetary policy. Suggesting that this is merely a correction to earlier excessive strength.
UK (GBP)	5	4	BoE has noted impact of stronger GBP on inflation forecasts, but it has not felt central to the debate. More recently, some concern that strong GBP is undermining rebalancing of UK economy away from domestic consumption.
Switzerland (CHF)	10	10	Interventionist but to prevent currency strength rather than actively target currency weakness.
Norway (NOK)	2	1	A year ago, NOK strength being offset with rate cuts. Now, the Norges Bank appears more relaxed about currency strength but still says has room to act.
Sweden (SEK)	1	2	Riksbank deputy governor Lars Svensson said it would be good for the wider economy if the Swedish Krona weakened. Deputy Governor Ekhol also said that the Central bank has the ammunition to prevent Krona gains
Canada (CAD)	0	0	Scaled back growth forecasts in January meeting and said that exports should remain below their pre-recession peak until the second half of 2014 owing to the persistent strength of the Canadian dollar.
Australia (AUD)	1	1	In the latest meeting they mentioned that the AUD remains high but they haven't expressed any real worry at the level of the exchange rate
New Zealand (NZD)	1	1	Wheeler talked down the prospect of intervening in currency markets and ruled out QE, he also said the reduction in interest rate has minimal effect on NZD.
Latam			
Mexico (MXN)	0	0	In late 2011 the FEC introduced a new mechanism to prevent excessive MXN weakness. There are no measures to resist MXN strength.
Argentina (ARS)	9	9	Central bank intervenes regularly to weaken the nominal exchange rate to maintain FX competitiveness
Brazil (BRL)	9	7	A year ago most intervention was aimed at weakening the BRL; now it is more two-way, keeping USD-BRL range-bound
Chile (CLP)	2	3	BCCH halted USD buying in late 2011; it is being considered again, but the CB board appears split
Columbia (COP)	4	8	Both the central bank and the government (via SWF management) intervene to buy USDs and prevent excessive COP strength
Peru (PEN)	4	7	Steady intervention is used to slow, but not reverse, the pace of PEN strength; more two-way volatility is desired by BCRP
Venezuela (VEF)	7	8	Tight FX controls limit the ability to conduct FX transactions. In addition, the government has just announced a devaluation to 6.3 from 4.3 against the USD.
EMEA			
Czech Republic (CZK)	4	5	CNB envisages intervening directly in the FX to weaken the currency
Hungary (HUF)	2	2	Rather relaxed so far, the NBH may target a weaker HUF when the new governor will be appointed in March
Russia (RUB)	5	3	The CBR has still an exchange rate target but a liberalisation is underway with the target of a pure free float in 2015
Romania (RON)	6	6	It's a managed float and the NBR's tolerance for any substantial appreciation/depreciation is limited.
Turkey (TRY)	8	8	CBRT targets the REER. It uses the interest rate corridor and RRR to counter any TRY rise
Poland (PLN)	1	1	The NBP keeps an orthodox monetary policy approach. Intervention (if any) would be sporadic
Israel (ILS)	4	4	The ILS plays an important role for the BoI. Risk of intervention to fight ILS appreciation exists
South Africa (ZAR)	0	0	Risk of intervention practically non-existent

Source: HSBC

	Currency war appetite		Description of attitude towards FX and tools (if any) being used to target FX
	Jan 2012 score	Jan 2013 score	
Asia			
China (CNY)	6	4	The PBoC does intervene in the onshore spot FX market, though it has become increasingly "hands-off". The FX rate is still largely controlled by the setting of the daily USD-CNY fix, but the FX regime is becoming increasingly liberalised and market driven.
Hong Kong (HKD)	2	2	Hong Kong operates a fully pegged exchange rate regime, with the HKD managed mechanistically between 7.75-7.85 versus the USD. Since October 2012, the HKMA has bought nearly HKD90bn to prevent the HKD from strengthening outside of the band versus the USD. But the intervention seen by the HKMA does not indicate that policy makers are actively pursuing a weaker currency - it is simply a function of Hong Kong's financial system.
Taiwan (TWD)	8	7	Defensive against TWD appreciation via spot market intervention; tolerance shifts depending on competitor currencies' movements
South Korea (KRW)	7	6	Intervention and smoothing operations in both the FX spot and forwards markets, alongside and macro prudential measures. Policy makers have been stepping up their use of regulatory measures (such as capping FX forward positions for banks) but many new measures are aimed more at limiting volatility and external exposure than at limiting appreciation. There is a sense of an increasing tolerance of FX appreciation under the new government.
India (INR)	1	1	The RBI intervenes lightly via both FX spot and forwards markets to prevent sharp movements in the currency. In recent months, due to improving capital account flows, RBI has been building FX reserves when permitted by market conditions, but is not aggressively combating FX strength.
Indonesia (IDR)	1	1	BI is different from most Asian central banks as it has actually been combating IDR weakness rather than strength. But BI has only been supplying limited amount of USDs onshore to ease IDR weakness. With FX reserves quite low by regional standards, BI will likely buy USDs via the FX spot and forwards market to build FX reserves when permitted by market conditions, but will not actively pursue a weaker currency for the time being.
Malaysia (MYR)	3	3	BNM occasionally intervenes in the markets largely via FX spot and more rarely through FX forwards purchases/sales in order to smooth excess moves. Overall, BNM has been relatively permissive of MYR strength.
Philippines (PHP)	4	5	BSP actively smoothes FX appreciation through the FX spot and forward markets, alongside macro prudential measures. Has increasingly used regulatory measures to try to clamp down on "speculative" inflows, but with relatively little impact on the PHP. Occasionally employs "unconventional" use of its forwards book to squeeze USD liquidity onshore and weaken the PHP.
Singapore (SGD)	2	2	Unique FX policy sees the MAS buy USD-SGD if the SGD NEER pushes too close to the top of the NEER band on a daily basis. FX forward operations to squeeze onshore USD liquidity are occasionally used to weaken the SGD. However, the SGD NEER remains on a path of gradual appreciation suggesting MAS is willing to allow SGD to strengthen to combat inflationary pressures.
Thailand (THB)	3	3	The BoT intervenes in both the FX spot and forwards markets to manage broader volatility in the THB, though overall intervention has fallen. Pays attention to the movements in the THB REER and NEER, and broadly looks for THB strength to be reflective of fundamentals and not out of line with the rest of the region. Last year reiterated regulations with regards using FX forwards for hedging of non-underlying activity. Aiming to liberalise outflows as a way of balancing inflow pressures.
Vietnam (VND)	2	2	The SBV sets a daily fix which has been unchanged since 24 December 2011 (so effectively a USD peg has been in place since then) with a 1% daily trading band around the fix. SBV has appeared to be buying USD-VND within the band to bolster its relatively low level of FX reserves, but is not actively pursuing a weaker currency.

Source: HSBC

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