

# **Renminbi Revaluation, Euro Appreciation and Chinese Markets: What Can We Learn From Data?**

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## **Summary**

This paper examines daily financial market data available from Reuters from 2003-2004 (before the recent revaluation) to assess the likelihood of RMB revaluation and its implications for Series A Chinese share price movements, given the continuing appreciation of the Euro against the US dollar.

The movements of non-deliverable forward (NDF) premia or discounts are the key financial market indicators linking the appreciation of the Euro with changes in Chinese asset prices. When the Euro appreciates relative to the US dollar, the NDF premia decrease (or discounts increase). These NDF movements in turn lead to movements in the Series A share prices.

Our results also show that interest rate differentials between Chinese three month securities and the US Federal Funds rate play little role in this process. They neither respond to Euro appreciation, nor do they significantly affect movements in NDF premia and Series A share prices.

We find these empirical results to be quite robust to alternative empirical methods based on traditional vector autoregressions (known as VARs) and Bayesian adaptations of this methods (known as BVARs). The results are also robust to tests based solely on in-sample estimation as well as tests based on out-of-sample forecasting methods. Finally, while both the VAR and BVAR methods deliver similar results, the BVAR method is more effective for out-of-sample forecasting accuracy, relative to the more widely used VAR approach.