



*R&R Weekly Column*  
*By Brunello Rosa*



## Trade War Fears Continue Weighing on Investor Sentiment


Last Friday, equity markets sold off sharply on the back of the lower-than-expected NFP figures (103K jobs added in March, versus 193K expected) and renewed trade war fears. The below-consensus NFP figure need to be considered on a multi-month basis and could have been expected, to some extent, after the sharp 313K increase recorded last month (more than 100K above consensus). So the March figures don't need to be considered per se as a sign of a weakening labour market, especially after Fed Chairman Jay Powell said (earlier last week), that subdued wage growth signals that [the US labour market "is not excessively tight."](#) A *fortiori*, this month's NFP figures cannot be considered indicative of an imminent slowdown of the US economy, which might, in fact, be in acceleration phase, partly as a result of the fiscal stimulus imparted by the tax cuts and the fiscal spending deliberated by the US administration in the last few months.

More worrying is the impact that fears of a potentially escalating trade war between US and China is having on investor sentiment and equity price dynamics. After the initial move by the US (which threatened to impose 25% duties on 1333 products, worth around \$50bn, related to China's alleged theft of US intellectual property), and the initially modest retaliatory move by China, threatening to impose tariffs on (well-targeted) imports worth USD 3bn, the US has threatened to impose additional USD 100bn in tariffs on imports from China, when China threatened to impose tariffs on 106 products (including soybeans, cars and chemicals) worth USD 50bn. This tit-for-tat game (which, as history teaches, ends up destroying value for all sides, with no eventual winner) is unnerving market participants, who fear a full-blown trade war that could eventually spark a global recession.

Clearly, a trade war is not in the interest of either contender: the US cannot seriously threaten a major holder of its public and agency debt, without endangering its financial stability, and the value of the US dollar; China cannot seriously threaten a major buyer of its global exports, and the currency in which most of its foreign reserves are denominated. So, game theory would suggest that a solution can be found after the US administration would have symbolically proven that the US will not observe the rise of China as a strategic rival without reacting, and the promise by China to open up its markets over time; and after China would have proven to be the rising hegemonic power, able to call the US as the violator of WTO rules. But it will take time for that equilibrium to be reached. In the meanwhile, markets will remain jittery, and investor sentiment under the cosh.

In our [analysis](#) in February, we discussed how hard it will be for equity markets to return to the January peaks, and recent developments seem to confirm that this will be the case. In such an environment, our [updated pro-forma strategic asset allocation](#) continues to favour a moderate risk taking within a defensive positioning, with slightly greater exposure to sovereign bonds and lower to commodities.

### **Our Recent Publications**

 [\*\*Asset Allocation Update: Cautious Risk Exposure With Defensive Positioning,\*\*](#) by Francisco Quintana and Alessandro Magnoli Bocchi, 29 March 2018

 [\*\*Transition Deal, Trade Agreements and Risks of a Cliff-Edge into WTO.\*\*](#) by Brunello Rosa, Pablo Gallego Cuervo and Renata Bossini, 28 March 2018



The Week Ahead

**US - March inflation is expected to rise moderately.** CPI is expected to slightly accelerate (c: 2.3% y-o-y; p: 2.2%). The Fed will publish the minutes of the FOMC March 20-21 meeting. Chinese inflation is expected to decelerate (c: 2.7% y-o-y; p: 2.9%).

**Europe - Hungary will hold parliamentary elections.** The conservative, right-wing populist Fidesz party, led by PM Viktor Orban, is expected to keep its majority.

The Quarter Ahead

**US – Trade dispute with China likely to ease.** So far, only USD 4.3bn of US imports from China and USD 3.0bn of Chinese imports from the US are subject to new tariffs. Eventually, the willingness to negotiate shown in previous weeks will prevail. In North America, a preliminary deal to update NAFTA could be agreed in next week's summit.

**Western diplomatic relations with Russia will stay frosty.** The US imposed new sanctions on 38 individuals and companies believed to be close to President Putin.

**India -** In the first half of the 2018-19 FY the government will reduce its borrowing, creating a short-term supply squeeze.

**Iran - US pressure could result in the suspension of the nuclear deal.** The US waiver on Iran sanctions has to be renewed by May 12. The new US Secretary of State, Mike Pompeo, opposes the agreement.

**Syria - The country will continue to receive strong foreign support.** The presidents of Turkey, Iran and Russia met to continue their 15-month cooperation on Syria.

**Qatar – Will return to the bond market.** The QCB announced plans to issue in 2018 roughly the same amount of QAR-denominated debt issued in 2017, ~USD 13.1bn.

**Oil prices are likely to decline.** Brent oil prices fell by 4.5% w-o-w to USD/bbl. 67.1 amid trade war concerns. By year-end, Brent oil prices will likely decline to the USD/bbl 55-65 range: a growing non-Opec output will offset Saudi Arabia and Russia efforts to extend the Opec oil production agreement. Bahrain announced the discovery of an offshore deposit of shale oil, estimated to contain a total of 80bn barrels.

Last Week's Review

**US - Stocks posted losses following an escalation of tension in the US-China trade dispute.** Over the past week, the US: 1) released a list of proposed tariffs on imports from China worth USD 50bn (mostly high-tech products); and 2) announced that the president is considering additional tariffs worth USD 100bn. In response, China: 1) implemented 15-25% tariffs on imports from the US worth USD 3bn (128 products, mostly food and metals); 2) announced 25% tariffs on imports from the US worth USD 50bn (106 products, including soybeans, automobiles, chemicals and aircraft); and 3) the possibility of "new comprehensive countermeasures" against the US. US stocks reacted with losses—the S&P500 declined by 1.4% w-o-w—and volatility increased to 21.5 (+1.5 points w-o-w), below its long-term average of 22 points. US stock funds suffered outflows worth USD 10.0bn, and European funds saw outflows of USD 2.4bn. The 10-y UST yield rose 4bps w-o-w to 2.78% following hints on rising policy rates by the Fed's Chairman. The USD strengthened against a basket of currencies (DXY rose by 0.1% w-o-w) and the EUR (EUR/USD declined by 0.3% w-o-w to 1.229). **In March, US jobs growth eased.** Non-farm payrolls grew by +103k m-o-m (c: 193k; p: 313k). The unemployment rate remained steady at 4.1% (c: 4.0%; p: 4.1%).

**China - PMI declined:** China's March Composite PMI declined to a four-month low of 51.8 (p: 53.3).

**EZ - Inflation rose in line with expectations.** (March CPI a: 1.4% y-o-y; c: 1.4%; p: 1.1%).

**Egypt - President Sisi was officially re-elected for a second term.** Sisi secured 97.1% of the votes in the March 26-28 election (2014 election: 96.9%). Turnout declined to 41.1% (2014 election: 47.5%).

**Turkey - The TRY continued to depreciate.** The USD/TRY closed at 4.04 (+2.3% w-o-w). In March, the REER declined to 83.4 (p: 85.0), the lowest level since the start of the data series in 2003.

**Pablo Gallego Cuervo and Renata Bossini** contributed to this Viewsletter.

The picture in the front page comes from [this website](#)



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## Abbreviations, Acronyms and Definitions

<i>a</i>	<i>Actual</i>	<i>k</i>	<i>thousand</i>
<i>ann.</i>	<i>annualized</i>	<i>KRG</i>	<i>Kurdistan Regional Government</i>
<i>bn</i>	<i>Billion</i>	<i>KSA</i>	<i>Kingdom of Saudi Arabia</i>
<i>BCB</i>	<i>Central Bank of Brazil</i>	<i>LN</i>	<i>Northern League</i>
<i>BoC</i>	<i>Bank of Canada</i>	<i>MSS</i>	<i>Five Star Movement</i>
<i>BoE</i>	<i>Bank of England</i>	<i>m-o-m</i>	<i>Month-on-month</i>
<i>BoJ</i>	<i>Bank of Japan</i>	<i>mb/d</i>	<i>Million barrels per day</i>
<i>bpd</i>	<i>Barrels per day</i>	<i>MENA</i>	<i>Middle East and North Africa</i>
<i>bps</i>	<i>Basis points</i>	<i>mn</i>	<i>Million</i>
<i>c</i>	<i>Consensus</i>	<i>MPM</i>	<i>Monetary Policy Meeting</i>
<i>C/A</i>	<i>Current account</i>	<i>MSS</i>	<i>Five Star Movement</i>
<i>CB</i>	<i>Central bank</i>	<i>NAFTA</i>	<i>North-American Free Trade Agreement</i>
<i>CBK</i>	<i>Central Bank of Kuwait</i>	<i>OECD</i>	<i>The Organization for Economic Cooperation and Development</i>
<i>CBO</i>	<i>US Congressional Budget Office</i>	<i>Opec</i>	<i>Organization of Petroleum Exporting Countries</i>
<i>CBR</i>	<i>Central Bank of the Russian Federation</i>	<i>p</i>	<i>Previous</i>
<i>CBT</i>	<i>Central Bank of the Republic of Turkey</i>	<i>pw</i>	<i>Previous week</i>
<i>CDU</i>	<i>Christian Democratic Union of Germany</i>	<i>PCE</i>	<i>Personal Consumption Expenditures</i>
<i>CNY</i>	<i>Chinese Yuan</i>	<i>PM</i>	<i>Prime minister</i>
<i>CBT</i>	<i>Central Bank of the Republic of Turkey</i>	<i>PMI</i>	<i>Purchasing managers' index</i>
<i>CPI</i>	<i>Consumer Price Index</i>	<i>pps</i>	<i>Percentage points</i>
<i>CPC</i>	<i>Communist Party of China</i>	<i>QCB</i>	<i>Qatar Central Bank</i>
<i>CSU</i>	<i>Christian Social Union in Bavaria</i>	<i>QAR</i>	<i>Qatari Riyal</i>
<i>DFMGI</i>	<i>Dubai Financial Market General Index</i>	<i>QE</i>	<i>Quantitative easing</i>
<i>DJIA</i>	<i>Dow Jones Industrial Average Index</i>	<i>q-o-q</i>	<i>Quarter-on-quarter</i>
<i>d-o-d</i>	<i>Day-on-day</i>	<i>RBA</i>	<i>Reserve Bank of Australia</i>
<i>DXY</i>	<i>US Dollar Index</i>	<i>REER</i>	<i>Real Effective Exchange Rate</i>
<i>EC</i>	<i>European Council</i>	<i>SAMA</i>	<i>Saudi Arabian Monetary Authority</i>
<i>ECB</i>	<i>European Central Bank</i>	<i>SHCOMP</i>	<i>Shanghai Stock Exchange Composite Index</i>
<i>EIA</i>	<i>US Energy Information Agency</i>	<i>tb/d</i>	<i>Thousand barrels per day</i>
<i>EM</i>	<i>Emerging Markets</i>	<i>tn</i>	<i>Trillion</i>
<i>EP</i>	<i>European Parliament</i>	<i>TRY</i>	<i>Turkish Lira</i>
<i>EU</i>	<i>European Union</i>	<i>UAE</i>	<i>United Arab Emirates</i>
<i>EUR</i>	<i>Euro</i>	<i>UK</i>	<i>United Kingdom</i>
<i>EZ</i>	<i>Eurozone</i>	<i>US</i>	<i>United States</i>
<i>Fed</i>	<i>US Federal Reserve</i>	<i>USD</i>	<i>United States Dollar</i>
<i>FOMC</i>	<i>US Federal Open Market Committee</i>	<i>USD/bbl.</i>	<i>USD per barrel</i>
<i>FRB</i>	<i>US Federal Reserve Board</i>	<i>UST</i>	<i>US Treasury bills/bonds</i>
<i>FX</i>	<i>Foreign exchange</i>	<i>VAT</i>	<i>Value added tax</i>
<i>FY</i>	<i>Fiscal Year</i>	<i>VIX</i>	<i>Chicago Board Options Exchange Volatility Index</i>
<i>GCC</i>	<i>Gulf Cooperation Council</i>	<i>WTI</i>	<i>West Texas Intermediate</i>
<i>GBP</i>	<i>British pound</i>	<i>w-o-w</i>	<i>Week-on-week</i>
<i>GDP</i>	<i>Gross domestic product</i>	<i>y-o-y</i>	<i>Year-on-year</i>
<i>GOP</i>	<i>Grand Old Party (US Republican Party)</i>	<i>y-t-d</i>	<i>Year-to-date</i>
<i>IMF</i>	<i>International Monetary Fund</i>	<i>ZAR</i>	<i>South African Rand</i>
<i>IPO</i>	<i>Initial public offering</i>	<i>10-y</i>	<i>10 year</i>
<i>JPY</i>	<i>Japanese yen</i>		



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