

## MAKING SENSE OF *THIS* WORLD

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By Brunello Rosa



### Trump's Never-Ending Trade Wars: Germany Is Next In Line


On March 1th, the truce between US and China that was agreed to regarding their bilateral trade war will officially end, as will the time available to reach an agreement to avoid increasing tariffs from 10% to 25% on USD200bn of Chinese exports to the US. Officials from both sides seem to suggest that a deal might be in sight, nevertheless a number of issues will remain open. Most important of these is that any agreement will be temporary, as the underlying “cold war” between the US and China will continue to be waged on different battlefields, as we have discussed in [previous columns](#) and [research papers](#). In particular, the two countries will continue to compete intensely over technology (as [the ongoing Huawei case proves](#)).


In addition, the implementation of any plan to reduce the bilateral trade imbalance between China and the US [will not be frictionless](#). Regardless of whether China agrees to import more from the US, or export less to the US, there might be severe consequences on global trade flows, technological transfers, CNY and USD valuations, the level of Chinese reserves of US Treasuries, long-term US Treasury yields and, ultimately, global price and financial stability. The optimal strategy of pursuing global free trade with flexible exchange rates on a multilateral basis (for example by continuing to push China towards greater openness of its capital account) does not seem at hand in an increasingly protectionist world dominated by strongmen.


However, let us assume for the time being that some sort of deal between US and China is achieved by March 1<sup>st</sup>. Will this mean peace at last in the global economy? To the contrary, it will probably mean that, with one front temporarily closed, Trump will instead start devoting its full attention to another “trade war” close to his heart: the international auto sector, the most notable victims of which would be European and Asian producers, were the US to raise tariffs. In fact, President Trump will soon receive a report from the US Department of Commerce addressing his question of whether imports of cars pose a threat to national security. It is not yet known what the report, expected to be sent by February 17<sup>th</sup>, will recommend the president to do, [but it is very likely that it will offer a range of options](#), including imposing quotas or voluntary export restrictions, or tariffs. The one thing that Trump managed to obtain with [the transformation of NAFTA into USMCA](#) is less favourable conditions for producers to export cars to the US. He is likely to want to adopt a similar stance towards other car producers, particularly German ones.

In fact, it is almost certain that among the biggest losers of the upcoming round of trade wars will be Germany, the economy of which – as we discuss in [our recent trip report](#) – is already suffering from a deteriorated external environment. The slowdown in Germany is affecting the entire Eurozone economy, with the more fragile countries, [such as Italy](#), having already entered a recession. At the Munich Security Conference just concluded, [the US and Germany have further exposed the fact that they have opposing views regarding global security](#), as expressed by Chancellor Merkel and Vice-President Pence. We would not be surprised if a US trade war with Germany over the auto sector become just another example of geopolitical diplomacy, fought with different weapons.

#### Our Recent Publications

 [TRAVEL NOTES – ITALY: Risks Re-Emerging After The Truce](#), by Brunello Rosa, 15 February 2019

 [TRAVEL NOTES – Germany's Economic and Political Uncertainties Are Rising](#), by Nouriel Roubini and Brunello Rosa, 14 February 2019

 [POLICY COMPASS- Brexit Update: Getting to A Deal \(One Way or Another\)](#), by Brunello Rosa and Nouriel Roubini, 13 February 2019

**Looking Ahead**

**The Week Ahead: Global Growth Slowdown To Continue**

**In the US**, consumers might be less willing to spend, as signaled by the decline in December's retail sales (Retail sales Dec. a: -1.2% m-o-m; c: 0.2%; p: 0.1%).

**In the EZ**, February's manufacturing PMI is expected to remain flat (EZ Markit manuf. PMI Feb., c: 50.3; p: 50.5). Inflation is expected to remain stable at 1.4% (p: 1.4%).

**In Germany**, as investor confidence declines, the economic sentiment is expected to deteriorate (ZEW survey Feb. c: -18.4; p: -15.0).

**The Quarter Ahead: Brexit and China-US Trade Talks at The Forefront**

On March 1<sup>st</sup>, **the US-China trade-war** truce will officially end. After high-level talks, both governments signaled that they may be approaching a deal. President Xi Jinping stated: "the meetings achieved important progress". If no deal is reached, tariffs on USD200bn of Chinese imports will increase to 25% (p: 10%).

**In the UK**, the probability of no-deal Brexit is rising. By rejecting (303 votes to 258 — a majority of 45) a motion to support PM May's Brexit strategy, lawmakers weakened the PM's negotiating position with the EU. Large manufacturers urged the EU to: i) delay Brexit by six to 12 months, or ii) "make a clean break from Britain on March 29", supporting the PM's proposal to ensure an orderly UK departure.

**Last Week's Review**

**Real Economy: Global Slowdown Ongoing, Geopolitical Risks Remain High**

**In the US**, bipartisan lawmakers agreed to a spending deal of USD1.4bn, including physical barriers along the US-Mexico border - less than the USD5.7bn President Trump had demanded. To secure additional funding, President Trump declared "national emergency" - a move likely to spark controversies. The impact of the tax cuts passed in 2017 resulted in a higher-than-expected deficit, as reported in December's monthly budget statement (a: USD -14bn; c: USD -11bn; p: USD -205bn). **January CPI fell to 1.6%** (c: 1.5% y-o-y; p: 1.9%) given low energy prices; by remaining below the Fed's 2% target, it provided support to the Fed's "patience on potential rate hikes."

**In the US**, the probability of no Fed hikes in 2019 is at 98% (p: 97%); the probability of a rate cut declined to 10% (p: 18%).

**In the EZ**, data keep signalling a growth deceleration. Industrial production fell by 4.2% in December (c: -3.2% y-o-y; p: -3.0%).

**In Germany**, the economy stalled, falling short of entering a technical recession (a: 0.0%; c: 0.1%; p: -0.25%).

**In the UK**, growth and production disappointed (GDP Q4 a: 1.3% y-o-y; c: 1.4%; p: 1.6%; Industrial Production December a: -0.9% y-o-y; c: -0.4%; p: -1.3%). Inflation declined below the BoE's target for the first time in 2 years (January CPI a: 1.8% y-o-y; c: 1.9%; p: 2.1%).

**In China**, trade data showed stronger-than-expected exports (a: 9.1% y-o-y; c: -3.2%; p: -4.4%). Inflation fell to 1.7% (CPI January c: 1.9% y-o-y; p: 1.9%).

**Financial Markets: Lower Risks And CB Liquidity Are Supporting Asset Performance**

Global stocks ticked higher as fears over global trade and the possibility of another US government shutdown receded.

**Global stocks rose w-o-w** (MSCI ACWI, 1.9%) driven by the US (S&P 500, +2.5%) and the EZ (Euro Stoxx 50, 3.4%). EM indices declined (MSCI EMs, -0.5%). Volatility fell below historical averages (VIX S&P 500, 1.2 points to 14.9, 52w avg.: 17.0; 10y avg.: 18.1).

**Fixed-income indices remained flat** (BAML Global bond index, +0.0%). In DMs, German bunds have fallen 14 bps y-t-d to near-zero rates (10Y Bund yield, a: 0.10). In EM fixed income markets, the issuance volume declined w-o-w (a: USD 3.6bn; p: USD10.9bn). In Turkey, the Ministry of Finance hired banks to issue three-year Sukuk bonds.

**Currencies**: the USD rose (DXY, X+0.3%) the EUR fell (EUR/USD, 0.3% to 1.129). The GBP fell against the USD (GBP/USD, 0.4% to 1.289).

**Commodities**: EIA data showed US oil imports declining by nearly 1 mb/d w-o-w to 6.2 mb/d, increasing confidence in upcoming OPEC production cuts and driving oil prices (Brent) up by 6.7%, to 66.3 USD/bn.

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



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## Abbreviations, Acronyms and Definitions

a	Actual	LN	Northern League, Italy
AKP	Justice and Development Party, Turkey	MSS	Five Star Movement, Italy
ann.	annualized	m-o-m	Month-on-month
ARS	Argentinian Peso	mb	Million barrels
avg.	Average	mb/d	Million barrels per day
bn	Billion	MENA	Middle East and North Africa
BoC	Bank of Canada	MHP	Nationalist Movement Party, Turkey
BoE	Bank of England	mn	Million
BoJ	Bank of Japan	NAFTA	North-American Free Trade Agr.
bpd	Barrels per day	NATO	North Atlantic Treaty Organizat.
bps	Basis points	OECD	Organization for Economic Cooperation and Development
BS	Balance sheet	Opec	Organization of Petroleum Exporting Countries
c	Consensus	p	Previous
C/A	Current account	P2P	Peer-to-peer
CB	Central bank	PBoC	People's Bank of China
CBB	Central Bank of Bahrain	PCE	Personal Consumption Expenditures
CBK	Central Bank of Kuwait	PE	Price to earnings ratio
CBT	Central Bank of Turkey	PM	Prime minister
CDU	Christian Democratic Union, Germany	PMI	Purchasing managers' index
CNY	Chinese Yuan	pps	Percentage points
CPI	Consumer Price Index	pw	Previous week
DJIA	Dow Jones Industrial Average Index	QCB	Qatar Central Bank
DJEM	Dow Jones Emerging Markets Index	QAR	Qatari Riyal
d-o-d	Day-on-day	QE	Quantitative easing
DXY	US Dollar Index	q-o-q	Quarter-on-quarter
EC	European Commission	RE	Real estate
ECB	European Central Bank	RBA	Reserve Bank of Australia
ECJ	European Court of Justice	RRR	Reserve Requirement Ratio
EIA	US Energy Information Agency	RUB	Russian Rouble
EM	Emerging Markets	SWF	Sovereign Wealth Fund
EP	European Parliament	tn	Trillion
EPS	Earnings per share	TRY	Turkish Lira
EU	European Union	UAE	United Arab Emirates
EUR	Euro	UK	United Kingdom
EZ	Eurozone	US	United States
Fed	US Federal Reserve	USD	United States Dollar
FOMC	US Federal Open Market Committee	USD/b	USD per barrel
FRB	US Federal Reserve Board	UST	US Treasury bills/bonds
FX	Foreign exchange	VAT	Value added tax
FY	Fiscal Year	VIX	Chicago Board Options Exchange Volatility Index
GCC	Gulf Cooperation Council	WTI	West Texas Intermediate
GBP	British pound	WTO	World Trade Organisation
GDP	Gross domestic product	w	Week
IMF	International Monetary Fund	w-o-w	Week-on-week
INR	Indian Rupee	y	Year
IPO	Initial public offering	y-o-y	Year-on-year
IRR	Iranian Rial	y-t-d	Year-to-date
JPY	Japanese yen	ZAR	South African Rand
k	thousand	2y; 10y	2-year; 10-year
KSA	Kingdom of Saudi Arabia		



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