

MAKING SENSE OF *THIS* WORLD

21 September 2020



R&R Weekly Column
By Brunello Rosa



Towards A New Geo-Strategic Equilibrium In the Middle East

The [Abraham Accords Peace Agreement, signed](#) between United Arab Emirates, Bahrain and Israel in Washington last week, is aimed at the normalisation of the former two countries' diplomatic relations with Israel. It marks the shift towards various new geo-strategic equilibria being reached in the Middle East.

This process had begun in 2011, when the Obama administration started to withdraw US troops from Iraq. It continued in 2014, with the end of the US fighting mission in Afghanistan, and was then epitomised in 2015 by the Joint Comprehensive Plan of Action (JCPOA) signed between Iran and the five permanent members of the UN Security Council, plus Germany and the EU. Obama's aim, following Metternich's and (more recently) Kissinger's example, was that of creating a "balance of power" among the major countries in the region, to allow a gradual withdrawal of the US from the Middle East, which had become less strategically important since the beginning of the shale oil and gas revolution. To achieve that goal, Obama aimed at creating a balance of power between NATO (represented by Turkey), Sunni Muslims (Saudi Arabia), Jews (Israel) and Shia Muslims (hence the JCPOA with Iran).

The plan failed for two main reasons. First, as soon as the US started to withdraw from the region, Russia entered it with full force, becoming a decisive player. Second, the new US administration led by Trump reneged on the JCPOA and marginalised Iran in favour of the traditional US alliances with Israel and Saudi Arabia. This has led to an escalation of tensions with Iran, culminating in the [assassination of General Suleimani by the US at the beginning of 2020](#).


Between 2016 and 2020, the only two countries that managed to make serious advances in the region were Russia and Turkey, the two deciding in effect to [partition between themselves spheres of influence in Syria, Libya and the Eastern Mediterranean](#).

The Abraham Agreement marks the beginning of a new phase. First of all, the notion that in order to achieve a durable peace in the region, the Palestinian question needs to be addressed first, with the creation of two states between the Jordan River and the sea (deriving from the 1993 agreements in Oslo) has been wiped out. The logical order has been seemingly inverted. Rather than Palestinian statehood being a prerequisite to Sunni Arab states recognizing Israel, Sunni countries of the region will instead start normalising their relationship with Israel first, and this normalisation might eventually lead to the creation of a proper Palestinian state in the future.


Second, the fact that the US administration was actively involved in the mediation process via its secretary of State Mike Pompeo, and the fact that the agreement was signed in Washington, means that the US is still actively engaged in the process. In other words, only when a new geo-strategic regional equilibrium is reached the US may start to dis-engage. The Democratic candidate Joe Biden has committed to continuity of this approach as well.

Third, Turkey, as a NATO member, will be less able to play its own game in the region, having to abide by the superior interests of the US and of the alliance generally. Fourth, for the first time since 2015, Russia has been placed on the backfoot, and could not dictate its conditions. Finally, as it seems that many other countries in the region are now aiming at normalising their relationship with Israel as well, it is possible that this new, more pragmatic approach to a seemingly unsolvable problem might have the ability to lead to a new geo-strategic equilibrium being reached in the Middle East.

Our Recent Publications

 [A Brave New World: Why US Equity and Corporate Credit Markets are Overvalued and Overextended](#), by Peter Cecchini, 18 September 2020

 [Italian Regional Elections and Referendum Pose a Threat to The Government](#), by Brunello Rosa, 14 September 2020

 [Reviews: Fed, BoJ and BoE Leave Policy Stance Unchanged, But Add Important Twists To Language](#), by Brunello Rosa and Karmen Meneses, 17 September 2020

 [Flash Preview: US Federal Reserve Gradually Transitioning to a New Regime](#), by Nouriel Roubini and Farah Aladsani, 14 September 2020

Looking Ahead

The Week Ahead: US, EZ, Germany And Japan Manufacturing PMIs Continues To Expand, Whilst US Labor Market Weakens

In the US, EZ, Germany and Japan manufacturing and services PMIs are expected to remain in 'expansion'.

In the US, weekly data are likely to show a weakening labor market, with jobless claims rising to 3,500k (*p*: 860k). August durable goods orders are expected to decline to 1.5% m-o-m (*p*: 11.2%).

The Quarter Ahead: Geopolitical Risks Continue To Rise While CBs Remain Accommodative

Globally, inflation is likely to remain subdued over the next two years, but policy stimuli could lift it in the longer run.

Driven by COVID-19, new global patterns are emerging and will likely drive behavioral change: 1) working from home is on the rise; 2) online shopping is increasing; and 3) business travel is decreasing. The pandemic is further widening the rift between China and US.

In the US, the government banned the download of two popular Chinese-owned apps: i) TikTok, for video-sharing; and ii) WeChat, for messaging and electronic payments. According to US officials, the move - which drew objections for limiting free-speech rights - arises from "national security concerns". **Presidential candidate Joe Biden** is leading the polls, with the support of 50% of registered voters - while President Trump remains at 43%. The same polls suggest that: i) the Democrats are forecast to win both houses; and ii) Mr. Biden is ahead in Michigan, Pennsylvania and Wisconsin - three industrial states his Republican rival won in 2016 by a very thin margin, i.e.: less than 1%. **The Fed will refrain from rising interest rates**, until: 1) the economy reaches full employment; and 2) inflation hits the 2% target (likely to be years away), on track to "moderately exceed the target for some time".

In the EZ, a second wave of COVID-19 infections is likely to hamper confidence and slow the recovery; individual countries' performance will diverge, with Germany ahead of Italy or Spain.

In the UK, "if the EU fails to agree on a deal by December", President Boris Johnson intends to introduce a new legislation to "limit the EU's ability to influence customs arrangement and subsidies in Northern Ireland". In the BoE's meeting minutes the Bank stated it "would engage with UK regulators on how it might implement negative rates".

In China, the government launched a large-scale air and naval exercise in the South China sea, just as the US undersecretary Keith Krach was due to meet Taiwan's President Tsai Ing-wen. China's defense minister justified the action as "necessary to safeguard national sovereignty".

Last Week's Review

Real Economy: DM Consumption And Production Are Softening, China Rises. Central Banks Remained On Hold

In the US, in August retail sales increased by 0.6% m-o-m (*c*: 1.0; *p*: 0.9); July sales were revised downwards to 0.9% (*c*: 1.0), due to reduced unemployment benefits and lower policy support for small businesses. In August, IP decreased to a weaker-than-expected 0.4% m-o-m (*c*: 1.0; *p*: 3.5) and 7.7% y-o-y (*p*: 7.4), marking the 12th consecutive month of decline. The Fed kept its Fed funds target range unchanged at 0.0-0.25%.

In China, as the economy recovers from the COVID-19-induced shock, IP rose by 5.6% y-o-y (*c*: 5.1; *p*: 4.8) and *retail sales* increased by 0.5% y-o-y (*c*: 0.0; *p*: -1.1).

In Japan, the kept its policy stance unchanged, including its deposit rate at -0.1%.

In the UK, the BoE left the key interest rate unchanged at 0.1%.

Globally, all central banks reiterated their willingness to support the economic recovery, as necessary.

Financial Markets: S&P500's Third Consecutive Week Of Losses. Bonds Stable. Oil And Gold Up

Market drivers: risky assets made very gradual w-o-w gains - driven by EM equities and currencies, due to investors' concerns about the Fed's lack of guidance on how it will: 1) support the economic recovery; and 2) generate inflation through its balance sheet policy.

Global stocks remained flat w-o-w (MSCI ACWI, 0.0%, to 2,368), while US equities closed lower (S&P 500, -0.6% to 3,319), on declines in shares of technology companies. In Europe, despite positive economic data, stocks fell (Eurostoxx 50, -1.0% to 3,284), hampered also by renewed fears of a hard Brexit.

Fixed income: w-o-w, bonds were unchanged (BAML Global, 0.0% to 297.9), as well as the yield on US Treasury notes (10y UST, -0.1bps to 729.5).

FX: w-o-w, the USD, still suffering from unfavorable interest rate differentials, depreciated slightly against most currencies (DXY, -0.4% to 92.926; EUR/USD, -0.1% to 1.184).

Commodities: oil prices rose (Brent, 8.3% to 43.2 USD/b), after Saudi Arabia hinted at new production cuts. Gold rose (+0.4% to 1,950 USD/Oz.), supported by safe heavens inflows. Driven by China's economic revival, most industrial metals prices are above their pre-COVID-19 levels.



@RosaRoubini



Rosa & Roubini



Rosa&Roubini Associates

For more information, please call us on +44 (0)207 1010 718 or send us an email to info@rosa-roubini-associates.com

www.rosa-roubini-associates.com

118 Pall Mall, London SW1Y 5ED

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



Rosa & Roubini Associates Ltd is a private limited company registered in England and Wales (Registration number: 10975116) with registered office at 118 Pall Mall, St. James's, London SW1Y 5ED, United Kingdom. VAT registration number GB 278 7297 39. **Analyst Certification:** We, Brunello Rosa and Nouriel Roubini, hereby certify that all the views expressed in this report reflect our personal opinion, which has not been influenced by considerations of Rosa & Roubini Associates's business, nor by personal or client relationships. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the views expressed in this report. **Disclaimer:** All material presented in this report is provided by Rosa & Roubini Associates-Limited for informational purposes only and is not to be used or considered as an offer or a solicitation to sell or to buy, or subscribe for securities, investment products or other financial instruments. Rosa & Roubini Associates Limited does not conduct "investment research" as defined in the FCA Conduct of Business Sourcebook (COBS) section 12 nor does it provide "advice about securities" as defined in the Regulation of Investment Advisors by the U.S. SEC. Rosa & Roubini Associates Limited is not regulated by the FCA, SEC or by any other regulatory body. Nothing in this report shall be deemed to constitute financial or other professional advice in any way, and under no circumstances shall we be liable for any direct or indirect losses, costs or expenses nor for any loss of profit that results from the content of this report or any material in it or website links or references embedded within it. The price and value of financial instruments, securities and investment products referred to in this research and the income from them may fluctuate. Past performance and forecasts should not be treated as a reliable guide of future performance or results; future returns are not guaranteed; and a loss of original capital may occur. This research is based on current public information that Rosa & Roubini Associates considers reliable, but we do not represent it is accurate or complete, and it should not be relied on as such. Rosa & Roubini Associates, its contributors, partners and employees make no representation about the completeness or accuracy of the data, calculations, information or opinions contained in this report. Rosa & Roubini Associates has an internal policy designed to minimize the risk of receiving or misusing confidential or potentially material non-public information. We seek to update our research as appropriate, but the large majority of reports are published at irregular intervals as appropriate in the author's judgment. The information, opinions, estimates and forecasts contained herein are as of the date hereof and may be changed without prior notification. This research is for our clients only and is disseminated and available to all clients simultaneously through electronic publication. Rosa & Roubini Associates is not responsible for the redistribution of our research by third party aggregators. This report is not directed to you if Rosa & Roubini Associates is barred from doing so in your jurisdiction. This report and its content cannot be copied, redistributed or reproduced in part or whole without Rosa & Roubini Associates' written permission.

