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MAKING SENSE OF *THIS* WORLD

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R&R Weekly Column
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The "Blame Game" on Covid Masks Deeper Geopolitical Tensions

Last week, China announced that a number of boroughs in Beijing had to be locked down as a result of a new localised outbreak of Covid-19 in the city, possibly originating from another food market. The Chinese authorities said that investigations concluded that the coronavirus strain detected at the Xinfadi market in Beijing came from Europe, even if they admitted that this particular strain "has existed longer than the current coronavirus strain circulating in Europe."

So, it appears that China is now making accusations of other countries and regions for the possible second wave of pandemic it might be suffering. This is, of course, similar to the way most countries have accused China for having caused the pandemic in the first place, whether "naturally" (if the virus spread out the wet market in Wuhan), or "artificially" (either intentionally, or by accident, given the presence of the notorious research lab in Wuhan itself). What then should we make of this blame game between China and the rest of the world?

One should not be confused by the exchanges of allegations between politicians and even heads of state and governments. In most cases, these allegations are made to assuage the domestic opinion more than to attack the foreign entity, in order to distract attention and divert responsibility away from themselves. This is a usual game in politics. However, there is also something deeper going on now, which makes the current situation different from those which typically exist.

As we discussed a few weeks ago, we believe that after this pandemic, and after the containment measures that have been adopted to counter this pandemic, the world will look very different from how it was until the end of 2019. In particular, the economic or political power ranking of countries and regions could change on a global scale. For certain, the economic and political "distance" between the major global players will be very different: for example, China will be able to reduce the gap with the US on a number of dimensions. The US, with its erratic response to the pandemic, and its inability thus far to rein in the pandemic, will most likely lose ground versus China, whose response to the virus having been much more rapid and forceful. Europe is still debating which policies to adopt to recover from it.

The US and its closest allies in the Anglosphere (the so-called "Five Eyes": the USA, UK, Canada, Australia and New Zealand) are trying to respond this evolution of events. Clearly, the first point of attack is about the origin of the crisis, which is undoubtably in China; emphasizing this fact also serves to diminish the relevance of Beijing's strong response. For the first time in history, countries or state entities (such as Missouri and Mississippi) have expressed their intention to ask for "compensation" or "reparations" in non-war related circumstances, and this will continue to put pressure on China.

But there are other open fronts as well. As we know, the new Cold War between US and China has several components, one of which is the very relevant technological competition. Recently, the US imposed further restrictions on Chinese tech giant Huawei (which were subsequently partly eased). Countries in America's inner circle, such as Australia, have taken similar measures. This has meant a sharp deterioration in the bilateral relationships between Beijing and Canberra, even despite the fact that China has been the main importer of Australia's iron ore and coal in the last few years. But in the "new world order" of disrupted global supply chains, geopolitical considerations will trump economic cost/benefit analysis. This is an unfortunate evolution. It will eventually hurt the end consumer globally, as it will lead to a reduced choice of products and higher prices.

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Looking Ahead

The Week Ahead: US Nondefense Capital Goods Orders To Increase And Core-PCE Inflation Is Expected To Slightly Fall

In the US, May's 'nondefense capital goods orders' (ex. aircraft) is likely to rebound from contractionary territory, to 2.5% (*p:* -6.1%). PCE inflation is expected to remain unchanged at 0.5% y-o-y, while core-PCE inflation is likely to fall slightly, to 0.9% y-o-y (*p:* 1%).

The Quarter Ahead: Concerns Of A COVID-19 Second Wave and Weak Growth to Dominate the "Recovery" Phase

In the US, an increase in new infections and hospitalizations in a few States heightened concerns of a potential new wave of virus outbreak, raising worries over the potential implications for both the human and economic toll. The US 'Treasury Department', and 'Small Business Administration', stated they would '*disclose names and other details about businesses that take PPP loans of USD 150k or more*'. The Fed announced plans to: *i)* '*purchase individual corporate bonds in an effort to provide even more liquidity and stability to the credit markets*'; as well as *ii)* continue to make use of its full toolkit – including low interest rates and significant monetary stimulus – for an extended period of time, to help foster a lasting economic recovery. While US Secretary of State Pompeo met with Chinese officials, Trump signed into law an act that authorizes sanctions for Chinese officials involved in the detention of one million members of the Muslim Uighur minority ethnic group. ***Beijing*** quickly responded that the law *"maliciously attacks"* China and threatened consequences.

In the EZ, tensions with Beijing remain high, as MEPs called on the EU to consider a lawsuit against China over: *i)* the new Hong Kong law – defined as "*an assault on the city's autonomy*"; as well as *ii)* China's constant and increasing interference in Hong Kong's internal affairs. Over the next few months, EU leaders will try to: *1)* agree on a EUR 750bn (USD 840bn) 'recovery fund', renamed as 'Next Generation EU plan' - which could provide poorer and hardest hit EU countries with up to 15% of their GNI in grants and guarantees; and *2)* win the resistance of several northern European nations, which oppose the plan to pay out EUR 500bn (USD 559bn) in EU grants, and insist on loans instead.

Tensions between ***China and India*** rose after China accused Indian troops of a *"deliberate provocation"* in a deadly clash at a disputed Himalayan border.

In China, localized virus resurgence (e.g.: in Beijing) could morph into serious outbreaks. ***In Brazil,*** the number of COVID-19 cases surpassed 1.1m.

Last Week's Review

Real Economy: Geopolitical Tensions And Second-Wave Risks Threaten The Global Recovery

In the US, as stores reopened after the lockdown, May retail sales jumped by 17.7% m-o-m in (*c:* 8.0%), recovering from a record -14.7% fall in April - the biggest rise on record. As factories partially resumed operations after virus-related suspensions, May IP rebounded slightly, by 1.4% m-o-m, up from its record low (*c:* 2.9%; *p:* -12.5%); going forward, as supply chain restart, more manufacturing plants are likely to reopen. In the week ending on June 13, the number of US citizens filing for unemployment benefits eased slightly to 1.508m (*c:* 1.300m; *p:* 1.566m), the lowest level since the COVID-19 crisis began. However, u/e numbers are expected to rise at the end of the 'Paycheck Protection Program' (PPP) – i.e.: loans that help businesses keep their workforce employed.

In the EZ, May's CPI inflation remained mute at 0.1% y-o-y, and core-CPI inflation was unchanged from April's eight-month low of 0.9% y-o-y – well below the ECB's target of 'just below 2%'.

In Japan, UK, Switzerland, and Norway, all CBs kept key policy rates on hold and noted they stand ready to take any action needed to support the economy (BoJ: -0.10%; BoE: 0.10%; SNB: -0.75%; Norges Bank: 0.00%).

Financial Markets: EZ And US Stocks Rise, Bonds Flat; Oil Rebounds And Gold Maintains Appeal

Market drivers: stocks rebounded on better-than-expected economic data and stimuli efforts.

Stocks: w-o-w, global equity indices rose (MSCI ACWI, +2.0%, to 527), driven by the *EZ* (Eurostoxx 50, +3.7% to 3,269), lifted by the reopening of key economies, and the US (S&P 500, +1.9% to 3,098). EMs also rose (MSCI EMs, +1.5% to 1,001), driven by gains in China (Shanghai Comp., +1.6% to 2,968), despite the reported rise in COVID-19 new cases.

Bonds: fixed-income remained flat (BAML Global, +0.1% to 294.9), but investment-grade corporate bond credit spreads closed after the Fed stated it will begin '*buying individual corporate bonds to supplement its purchases of exchange-traded funds*'.

FX: w-o-w, the USD strengthened (DXY, +0.3% to 97.623) on positive retail sales data. The EUR keeps benefitting from policymakers' fiscal efforts.

Commodities: Oil prices rebounded (Brent, +8.9% to 42.2 USD/b), helped by: *i)* major oil-exporting nations adhering to production cuts; and *ii)* optimism over global demand. Gold rose slightly, driven by currency debasement fears (Gold, +0.8% to 1,743 USD/Oz.).

Farah Aladsani *contributed to this Viewsletter.*

The picture in the front page comes from this website

Abbreviations, Acronyms and Definitions

a	*Actual*
AKP	*Justice and Development Party, Turkey*
ann.	*annualized*
ARS	*Argentinian Peso*
avg.	*Average*
bn	*Billion*
BoC	*Bank of Canada*
BoE	*Bank of England*
BoJ	*Bank of Japan*
bpd	*Barrels per day*
bps	*Basis points*
BS	*Balance sheet*
c	*Consensus*
C/A	*Current account*
CB	*Central bank*
CBB	*Central Bank of Bahrain*
CBK	*Central Bank of Kuwait*
CBT	*Central Bank of Turkey*
CDU	*Christian Democratic Union, Germany*
CNY	*Chinese Yuan*
CPI	*Consumer Price Index*
DJIA	*Dow Jones Industrial Average Index*
DJEM	*Dow Jones Emerging Markets Index*
d-o-d	*Day-on-day*
DXY	*US Dollar Index*
EC	*European Commission*
ECB	*European Central Bank*
ECJ	*European Court of Justice*
EIA	*US Energy Information Agency*
EM	*Emerging Markets*
EP	*European Parliament*
EPS	*Earnings per share*
EU	*European Union*
EUR	*Euro*
EZ	*Eurozone*
Fed	*US Federal Reserve*
FOMC	*US Federal Open Market Committee*
FRB	*US Federal Reserve Board*
FX	*Foreign exchange*
FY	*Fiscal Year*
GCC	*Gulf Cooperation Council*
GBP	*British pound*
GDP	*Gross domestic product*
IMF	*International Monetary Fund*
INR	*Indian Rupee*
IPO	*Initial public offering*
IRR	*Iranian Rial*
JPY	*Japanese yen*
k	thousand
KSA	*Kingdom of Saudi Arabia*
LN	*Northern League, Italy*
M5S	*Five Star Movement, Italy*
m-o-m	*Month-on-month*
mb	*Million barrels*
mb/d	*Million barrels per day*
MENA	*Middle East and North Africa*
MHP	*Nationalist Movement Party, Turkey*
mn	*Million*
MPC	*Monetary Policy Committee*
NAFTA	*North-American Free Trade Agreement*
NATO	*North Atlantic Treaty Organization*
OECD	*Organization for Economic Cooperation and Development*
Opec	*Organization of Petroleum Exporting Countries*
p	*Previous*
P2P	*Peer-to-peer*
PBoC	*People's Bank of China*
PCE	*Personal Consumption Expenditures*
PE	*Price to earnings ratio*
PM	*Prime minister*
PMI	*Purchasing managers' index*
pps	*Percentage points*
pw	*Previous week*
QCB	*Qatar Central Bank*
QAR	*Qatari Riyal*
QE	*Quantitative easing*
q-o-q	*Quarter-on-quarter*
RE	*Real estate*
RBA	*Reserve Bank of Australia*
RRR	*Reserve Requirement Ratio*
RUB	*Russian Rouble*
SWF	*Sovereign Wealth Fund*
tn	*Trillion*
TRY	*Turkish Lira*
UAE	*United Arab Emirates*
UK	*United Kingdom*
US	*United States*
USD	*United States Dollar*
USD/b	*USD per barrel*
UST	*US Treasury bills/bonds*
VAT	*Value added tax*
VIX	*Chicago Board Options Exchange Volatility Index*
WTI	*West Texas Intermediate*
WTO	*World Trade Organisation*
w	*Week*
w-o-w	*Week-on-week*
y	*Year*
y-o-y	*Year-on-year*
y-t-d	*Year-to-date*
ZAR	*South African Rand*
2y; 10y	*2-year; 10-year*