

## Global risks escalate

Posted on May 17, 2019

The trade dispute has escalated in the last two weeks and looks set to be a war of attrition. This is not good for the Chinese economy, or the US economy. It is not good for global growth and will detract from the performance of more trade-dependent economies.

The trade dispute initially led to gains in alternative safe haven currencies, JPY, gold and CHF. EUR also firmed initially. However, the USD has regained the ascendancy in the last week. This may reflect some more solid US economic indicators creating the impression that the US remains resilient to the weaker impetus from abroad and the tariffs. It also reflects the drag on GBP and EUR from increased Brexit Chaos and rise of populists going into the EU parliamentary elections. The renewed weakness in EUR has probably spilled over to broader strength in USD against alternative safe-havens.

The CAD has been relatively stable on stronger economic reports and firmer oil prices. News that the US is removing steel and aluminium tariffs on its USMCA partners is also good news for CAD.

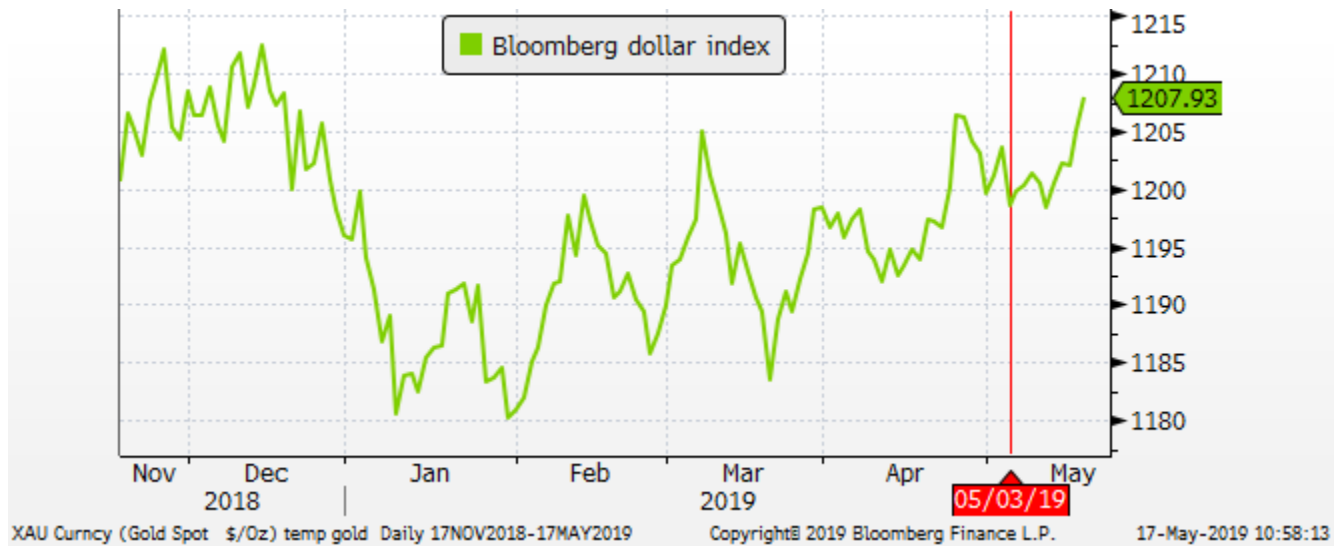
AUD has sunk in the last week after disappointing Australian economic data raised the prospect of rate cuts by the RBA. Weak Chinese economic reports also weighed on the AUD, although steel production growth rose to a new high in several years, consistent with Chinese stimulus and support for the real estate market. Iron ore prices rose to new high and Australian equity out-performed Asian and Major economies' equities. A weaker CNY on the trade dispute is trading down Asian currencies in general, including the AUD.

Threats to global investor confidence include tensions between the US and Iran. Combined with the trade war between the US and China, and Brexit chaos, there appears to be good reasons for the market to be trimming exposure to high beta assets (equities, high yield credit, EM markets) and increasing exposure to safe haven currencies – Gold and JPY. Bond yields and rate expectations are behaving more rationally, with yields falling.

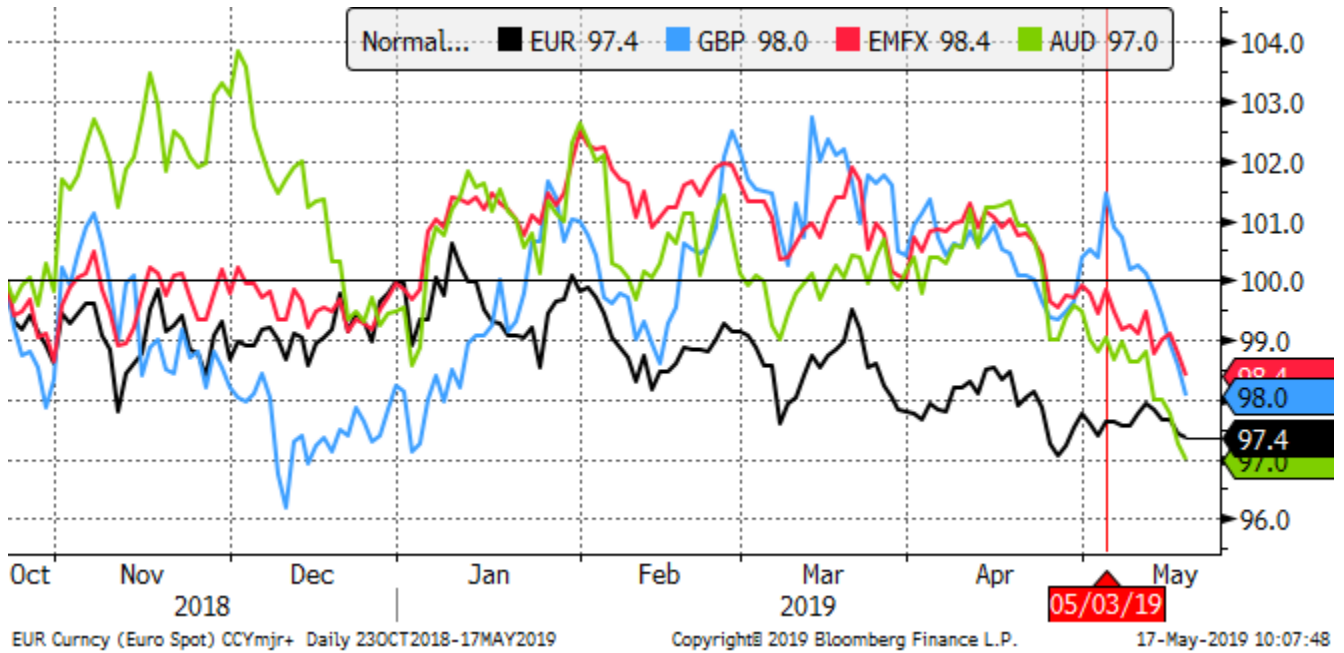
It is hard to say that the USD should continue to strengthen when US yields have fallen more than most other countries in recent weeks. But at this stage, there are few other alternatives. Gold seems to be an obvious choice, especially if China were to respond to their dispute with the US by seeking an alternative for their US Treasury holdings.

Global market developments since the US-China Trade tensions escalated over the last two weeks

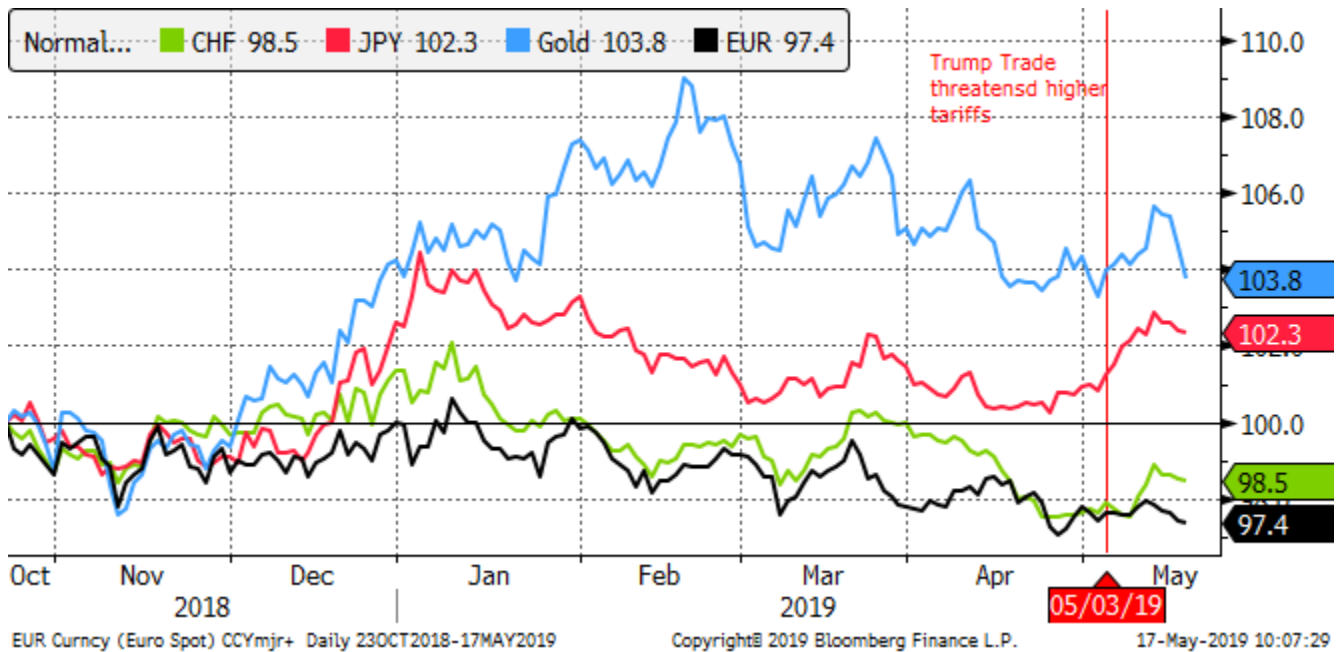
US equities weaker, US yields lower, USD stronger



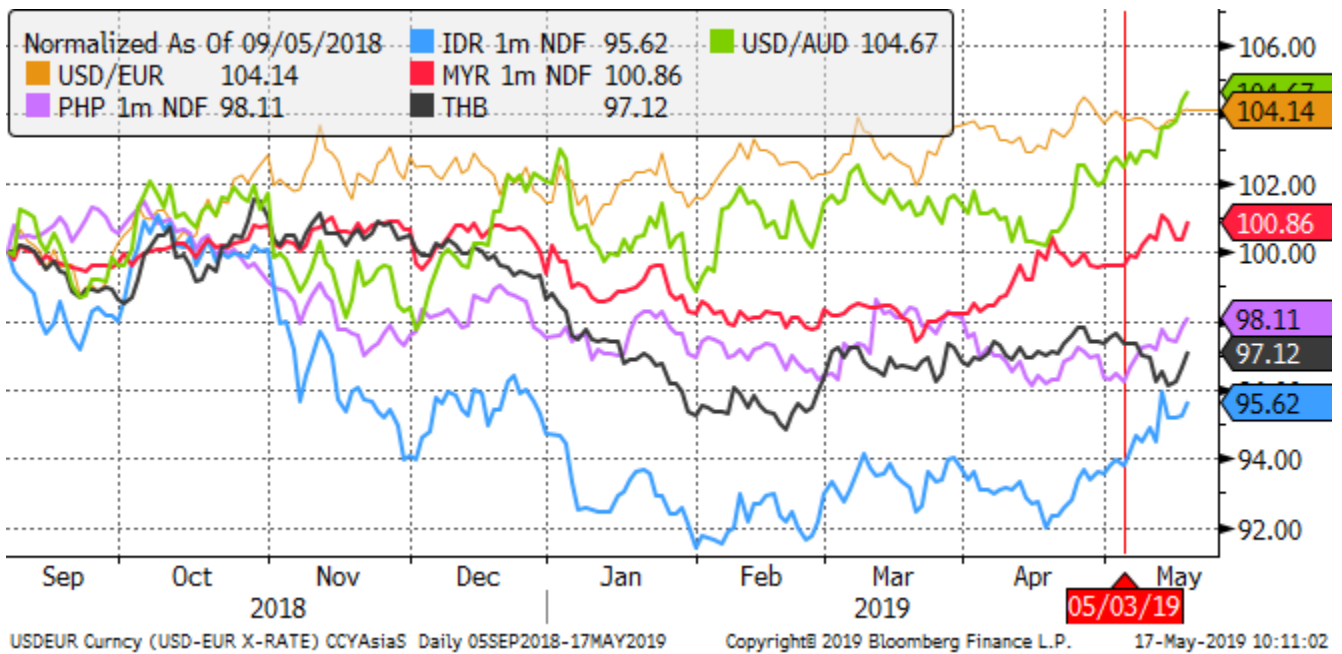
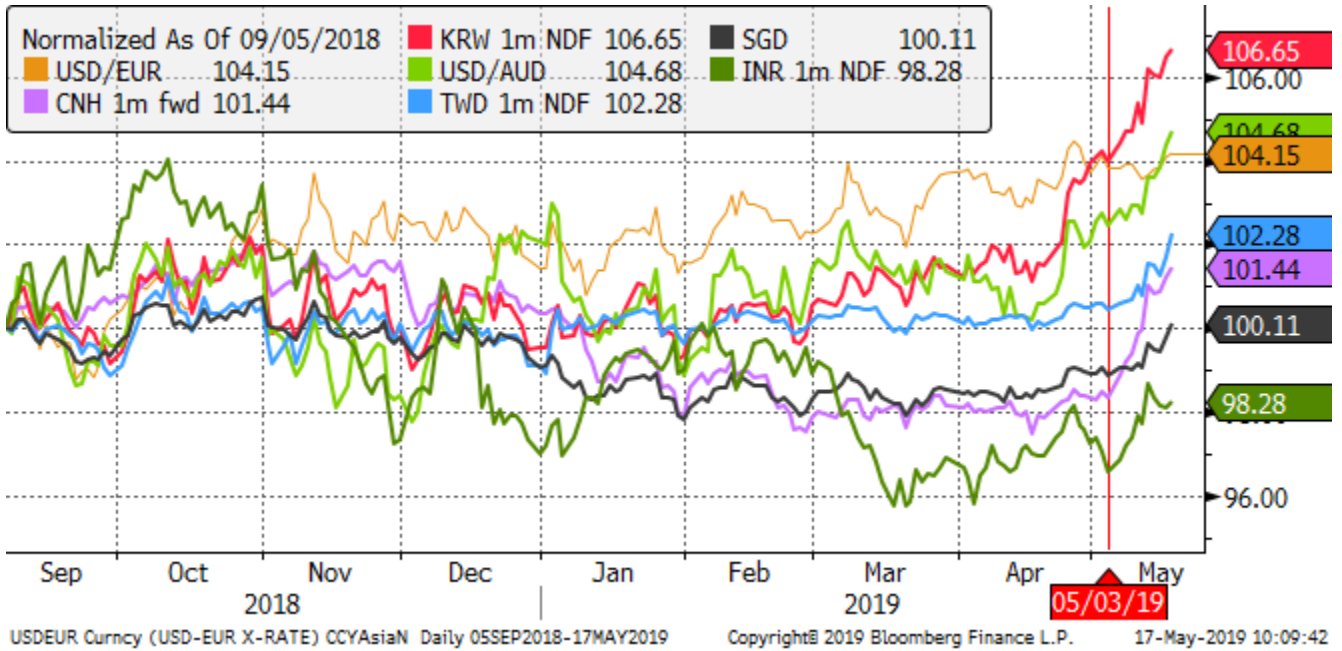
GBP down sharply in renewed Brexit chaos



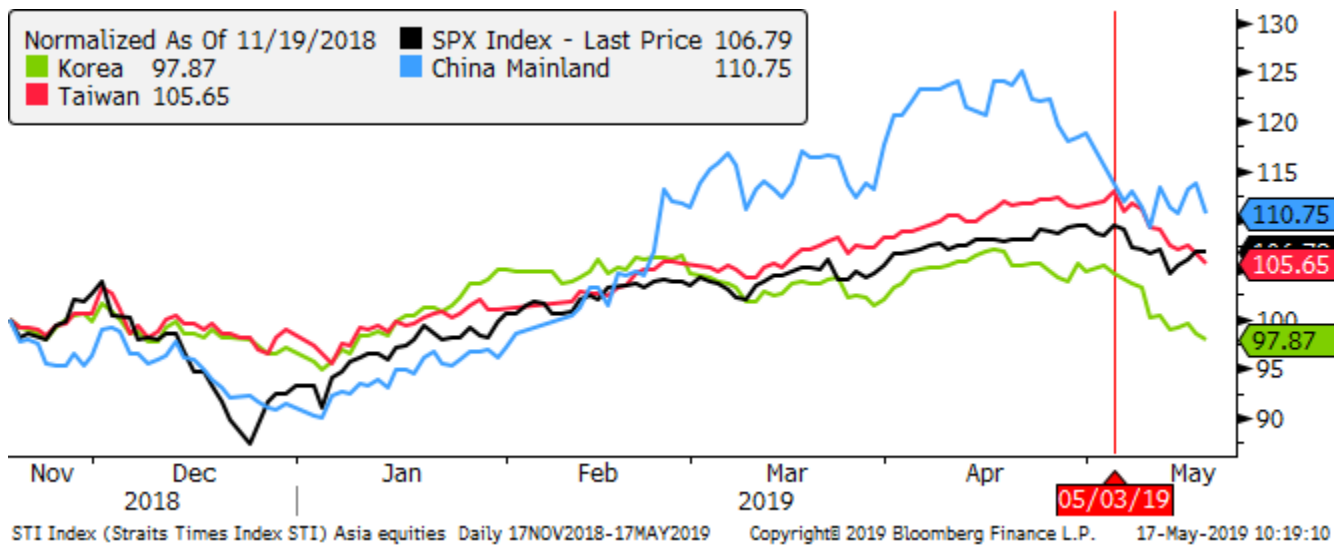
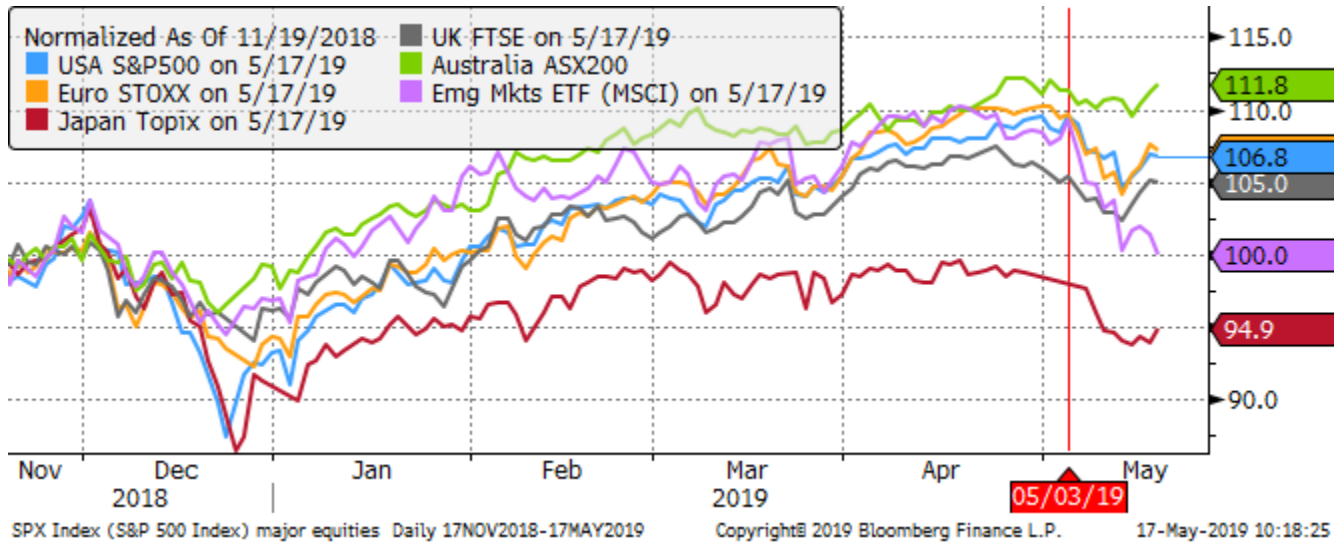
Safe haven currencies stronger, but reverse some gains in the last week



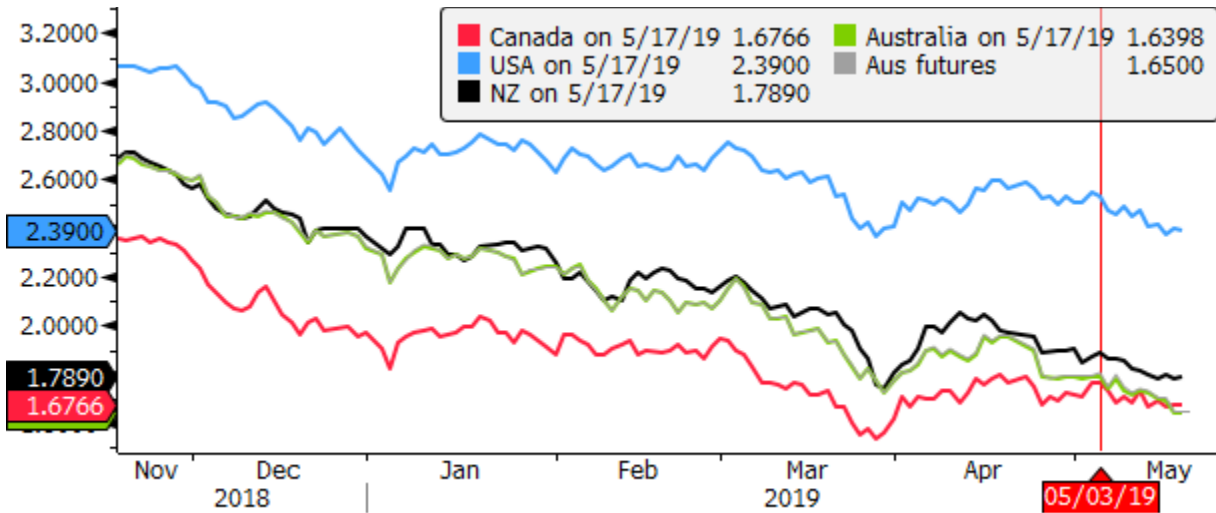
CNY falls and drags down other Asian currencies



Global equity markets weaker, although major equity markets recover partially in the last week, Australian equities strengthen supported by higher material sector equities

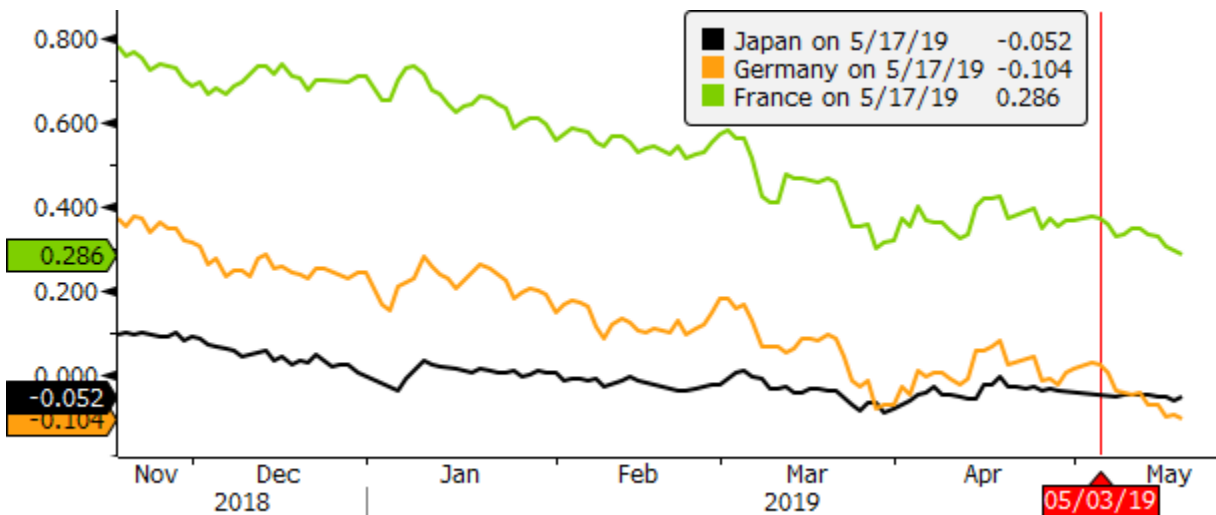


**10-year government bond yields fall, approaching or making new lows. Australian yields fall below Canada yields**



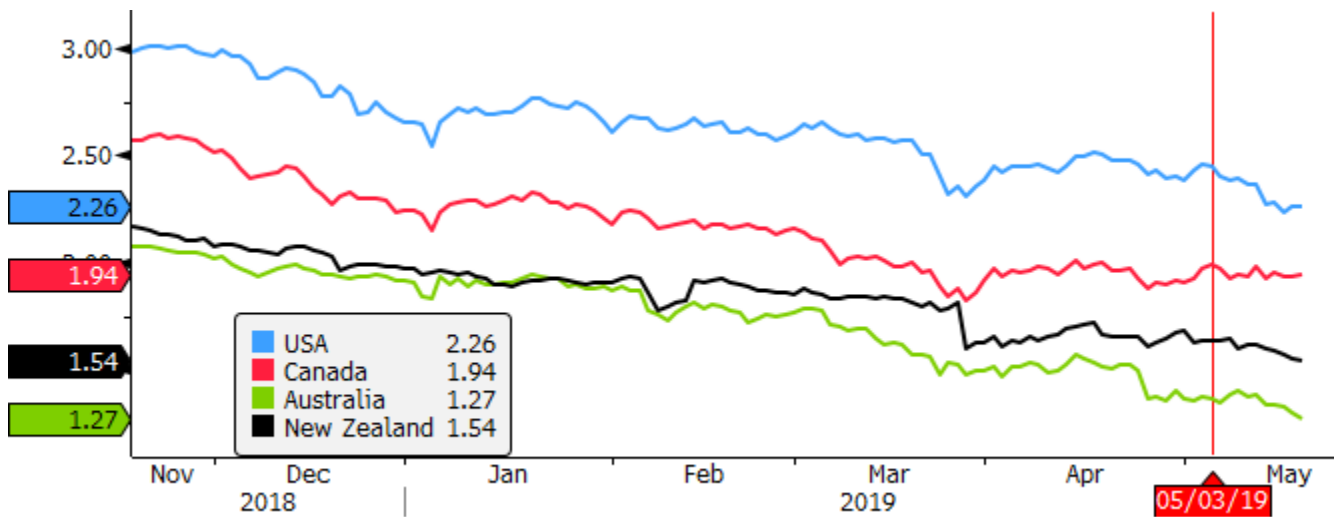
GJGB10 Index (Japan Generic Govt 10Y Yield) 10 year yields Daily 17NOV2018-17MA Copyright© 2019 Bloomberg Finance L.P. 17-May-2019 10:24:37

**German yields fall below Japan yields**

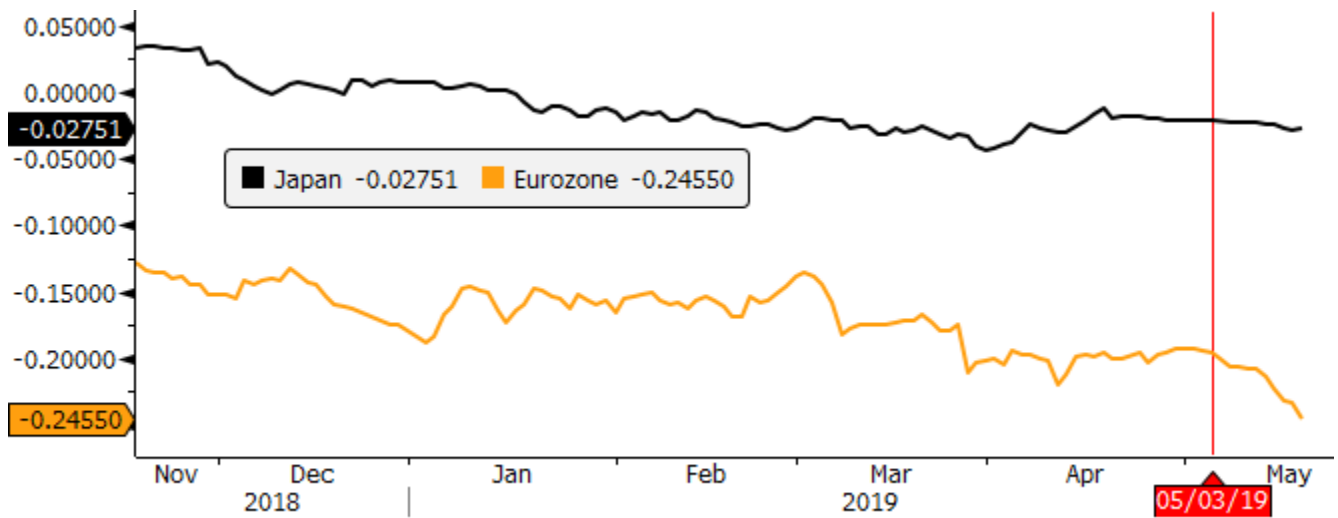


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2yr swap rates – rate expectations fall; significant in the US, Australia and Germany



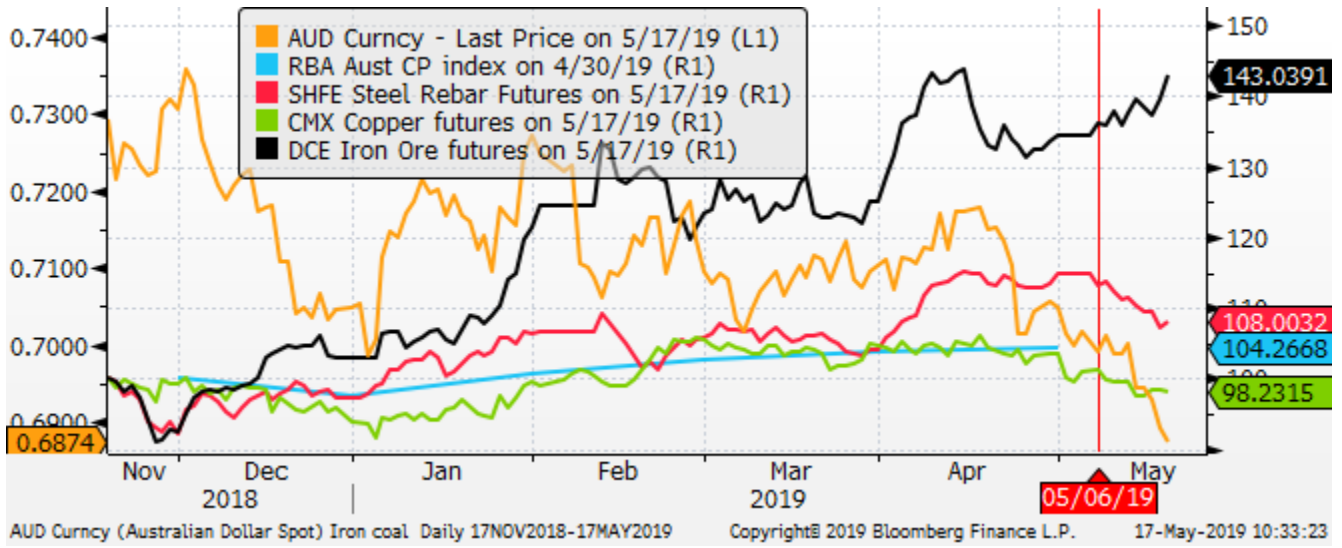
JYSW2 Curncy (JPY SWAP SA (V 6M) 2Y) 2yr swap rates Daily 17NOV2018-17MAY2019 Copyright© 2019 Bloomberg Finance L.P. 17-May-2019 10:29:52



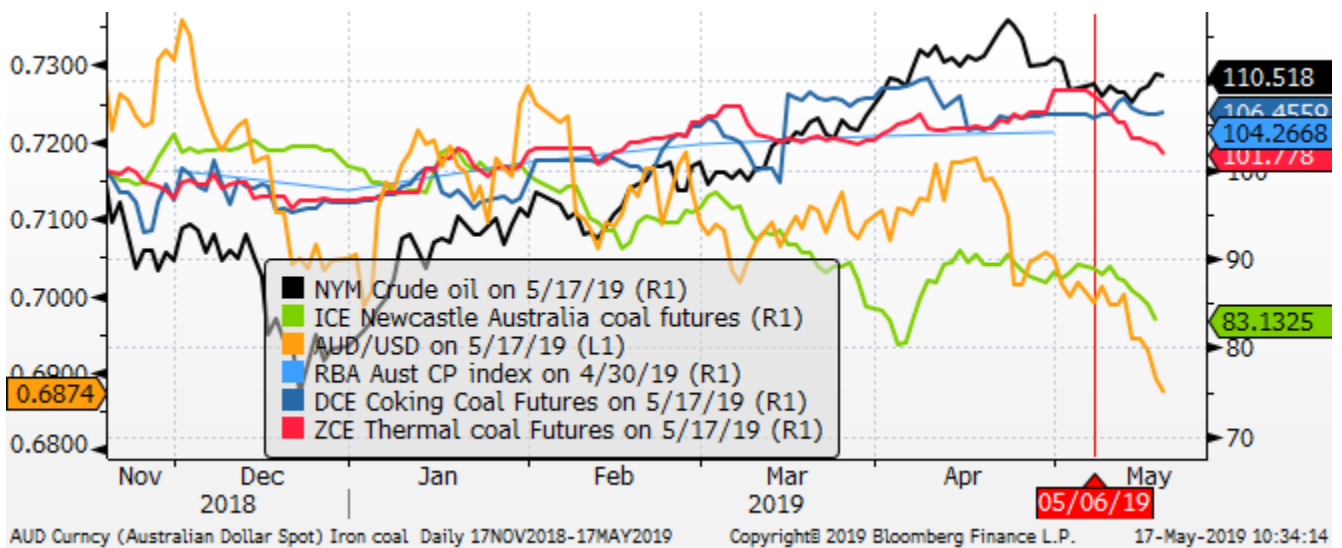
JYSW2 Curncy (JPY SWAP SA (V 6M) 2Y) 2yr swap rates Daily 17NOV2018-17MAY2019 Copyright© 2019 Bloomberg Finance L.P. 17-May-2019 10:29:40



Iron ore prices rise to revisit previous highs, modest falls in copper and steel prices

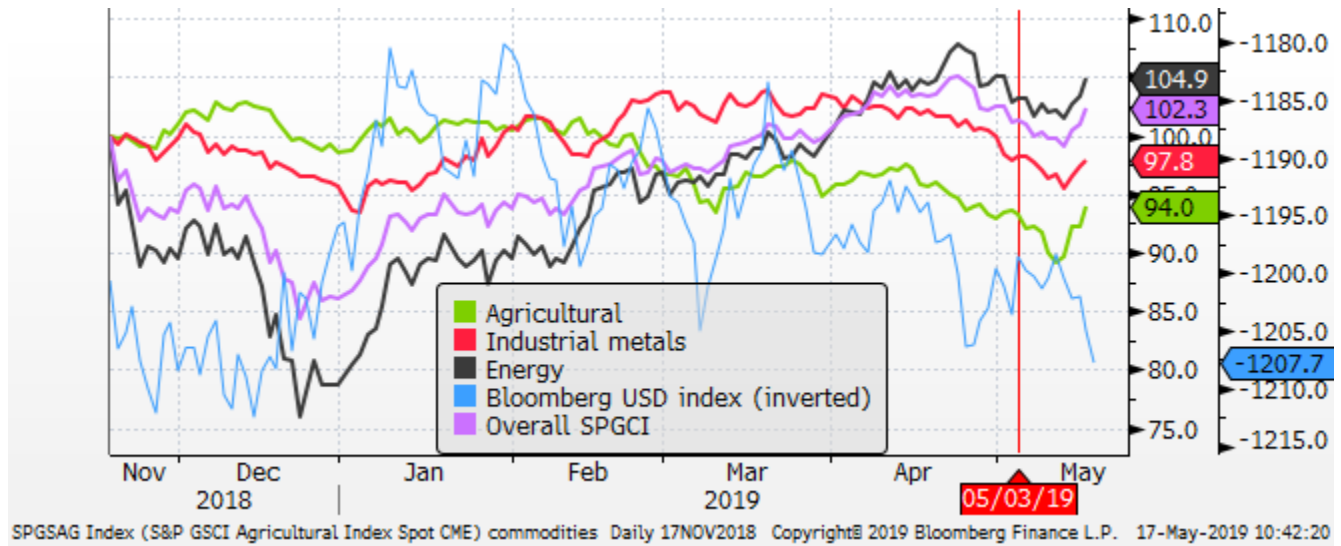


Oil prices and coking coal prices stable, thermal coal prices modestly weaker





Broad commodity price indices were weaker initially, but have recovered in the last week, despite a stronger USD



The recovery in US and major economy equities this week has taken the edge of gains in safe haven currencies. Gold, perhaps surprisingly, retraced all earlier gains.

However, our view on the US-China trade and economic tensions are that they are revealing major long term strategic goals, and there is no easy fix. As a result, we see ongoing softness in the global economy, and negative feedback to global equities.

Similarly, the Brexit process is deeply mired in political deadlock, and the market may get more despondent.

We see limited scope for a further rebound in global equities, and greater risk of waning global growth expectations dragging down equities in coming weeks. This may see support for safe haven currencies return.

Despite the steep falls in CNY and GBP in recent weeks, there is little reason to expect a recovery in either currency. This may prove an ongoing drag on EUR and AUD.

#### Disclosure and Certification

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