

Markets revert to trade war trend

Markets revert to classic "Trade-risk off" pattern, with equities down, bond yields down, oil down, gold up.



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To our Hong Kong Readers - our best wishes

First of all, if you're reading this in Hong Kong, stay safe. The turmoil ongoing in what is one of the biggest financial hubs in the region is very concerning, and I hope we return to calm before very much longer.

Markets sour

Markets have reverted to what is looking like a classic "Trade-related risk-off" pattern. Equities are lower, bond yields are lower, oil is lower, gold is higher.

Interestingly, US President Trump is actually now expressing optimism that a trade deal with China can be done. Just not when. Hopes for something from the Osaka G20 meeting are very low indeed. Markets, however, are maybe responding less to the day by day switch in message, than to the ongoing grind that the existing situation is exerting. This may also be related to the threats of sanctions on Germany/Russia over NordStream2.

One of the things that caught my eye today was that the USD is appreciating again. This is a key part of the classic "Trade-related risk-off" market pattern. But very recently, US Treasury yields had reached such a low point that this part of the relationship looked as if it were breaking down. Clearly, the Nordstream 2 squabble is EUR negative, and we need to see what happens on a day

when this isn't hitting the newswires as hard. But the dollar-positive trade aspect seems to be back on.

US inflation unerwhelms

Although it might be a bit early to expect a rate cut just yet, yesterday's inflation undershoot in the US does add weight to the argument that cuts are coming. James Knightley has written about the [outcome and implications here](#). In his view, the June FOMC will be used to tee-up markets for a cut at the following meeting on 1 August. That could begin to put a dent in the dollar.

Asia Day Ahead

Eyes down for the region's most capricious data release - the Australian labour report. Probably even more unpredictable than US non-farm payrolls. The important figure to watch today is the unemployment rate. This is the thing the RBA reckons needs to reach 4.5% to start generating higher inflation and take them closer to their 2-3% target range (1.3% currently). A 0.1pp decline is predicted. But this hinges not only on the numbers of unemployed, which is itself a function of the numbers of jobs created but also on the participation rate. And that figure jumps around more than an angry kangaroo. Still, with markets taking an exceptionally aggressive view on the forthcoming RBA easing (a view we feel is substantially overdone), a drop in the unemployment rate could be quite positive for the AUD, even if it is the consensus view - it will be a low conviction consensus.

After softer than anticipated aggregate finance data yesterday from China, we have to wait until tomorrow for the next installment of their economic struggle, when industrial production, fixed asset investment, and retail sales will be released. Our Greater China Economist, Iris Pang [thinks the soft finance data this could be a harbinger for weaker activity](#).

Japan's Ministry of Finance Business survey helps frame where we ought to be looking for the 1 July Tankan survey. The large manufacturing index released today fell to -10.4. This is a hard figure to read. 2Q surveys invariably fall. But today's reading was considerably down on the -3.2 figure last year. The forthcoming Tankan survey will be important as a very bad figure could be an excuse for the government to shelve the consumption tax hike, scheduled for October this year.

(And from Prakash Sakpal) India's May CPI inflation of 3.1% YoY was in line with the consensus, while the April figure was revised up to 3% from 2.9%. 3.4% YoY industrial production growth in April was also a significant upside surprise given the consensus view for only 0.6% growth. This heralds a recovery in GDP growth in the current quarter from a 5-year low of 5.8% in the previous quarter. This data undermines the case for the RBI continuing on an easing path during the rest of the year after a total of 75bp of rate cuts.

India's current account balance data for 1Q19 is expected anytime from now until the end of the month. The consensus of a sharp narrowing of the deficit to \$6.1bn from \$16.9bn in 4Q18 will be positive for the INR if it is correct, though we see no reason for the currency to react to such a backdated figure amid high external trade uncertainty.

Author

Olivia Grace
Editor

olivia.grace@ing.com

Julian Geib

Junior Economist, Global Trade

julian.geib@ing.de

Zoltán Homolya

Economic research trainee

zoltan.homolya@ing.com

Amrita Naik Nimbalkar

Junior Economist, Global Macro

amrita.naik.nimbalkar@ing.com

Mateusz Sutowicz

Senior Economist, Poland

mateusz.sutowicz@ing.pl

Alissa Lefebre

Economist

alissa.lefebvre@ing.com

Deepali Bhargava

Regional Head of Research, Asia-Pacific

Deepali.Bhargava@ing.com

Ruben Dewitte

Economist

+32495364780

ruben.dewitte@ing.com

Kinga Havasi

Economic research trainee

kinga.havasi@ing.com

Marten van Garderen

Consumer Economist, Netherlands

marten.van.garderen@ing.com

David Havrlant

Chief Economist, Czech Republic

420 770 321 486

david.havrlant@ing.com

Sander Burgers

Senior Economist, Dutch Housing

sander.burgers@ing.com

Lynn Song

Chief Economist, Greater China

lynn.song@ing.com

Michiel Tukker

Senior UK & Eurozone Rates Strategist

michiel.tukker@ing.com

Michal Rubaszek

Senior Economist, Poland

michal.rubaszek@ing.pl

This is a test author

Stefan Posea

Economist, Romania

tiberiu-stefan.posea@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Jesse Norcross

Senior Sector Strategist, Real Estate

jesse.norcross@ing.com

Teise Stellema

Research Assistant, Energy Transition

teise.stellema@ing.com

Diederik Stadig

Senior Economist, Healthcare & Technology

diederik.stadig@ing.com

Diogo Gouveia

Sector Economist

diogo.duarte.vieira.de.gouveia@ing.com

Marine Leleux

Sector Strategist, Financials

marine.leleux2@ing.com

Ewa Manthey

Commodities Strategist

ewa.manthey@ing.com

ING Analysts

James Wilson

EM Sovereign Strategist

James.wilson@ing.com

Sophie Smith

Digital Editor

sophie.smith@ing.com

Frantisek Taborsky

EMEA FX & FI Strategist

frantisek.taborsky@ing.com

Adam Antoniak

Senior Economist, Poland

adam.antoniak@ing.pl

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@ing.com

Coco Zhang

ESG Research

coco.zhang@ing.com

Jan Frederik Slijkerman

Senior Sector Strategist, TMT

jan.frederik.slijkerman@ing.com

Katinka Jongkind

Senior Economist, Services and Leisure

Katinka.Jongkind@ing.com

Marina Le Blanc

Sector Strategist, Financials

Marina.Le.Blanc@ing.com

Samuel Abettan

Junior Economist

samuel.abettan@ing.com

Franziska Biehl

Senior Economist, Germany

Franziska.Marie.Biehl@ing.de

Rebecca Byrne

Deputy Global Head of Editorial and Supervisory Analyst

rebecca.byrne@ing.com

Mirjam Bani

Sector Economist, Commercial Real Estate & Public Sector (Netherlands)

mirjam.bani@ing.com

Timothy Rahill

Credit Strategist

timothy.rahill@ing.com

Leszek Kasek

Senior Economist, Poland

leszek.kasek@ing.pl

Antoine Bouvet

Head of European Rates Strategy

antoine.bouvet@ing.com

Jeroen van den Broek

Global Head of Sector Research

jeroen.van.den.broek@ing.com

Edse Dantuma

Senior Sector Economist, Industry and Healthcare

edse.dantuma@ing.com

Francesco Pesole

FX Strategist

francesco.pesole@ing.com

Rico Luman

Senior Sector Economist, Transport and Logistics

Rico.Luman@ing.com

Jurjen Witteveen

Sector Economist

jurjen.witteveen@ing.com

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Nicholas Mapa

Senior Economist, Philippines

nicholas.antonio.mapa@asia.ing.com

Egor Fedorov

Senior Credit Analyst

egor.fedorov@ing.com

Sebastian Franke

Consumer Economist
sebastian.franke@ing.de

Gerben Hieminga

Senior Sector Economist, Energy
gerben.hieminga@ing.com

Nadège Tillier

Head of Corporate Sector Strategy
nadege.tillier@ing.com

Charlotte de Montpellier

Senior Economist, France and Switzerland
charlotte.de.montpellier@ing.com

Laura Straeter

Behavioural Scientist
+31(0)611172684
laura.Straeter@ing.com

Valentin Tataru

Chief Economist, Romania
valentin.tataru@ing.com

James Smith

Developed Markets Economist, UK
james.smith@ing.com

Suvi Platerink Kosonen

Senior Sector Strategist, Financials
suvi.platerink-kosonen@ing.com

Thijs Geijer

Senior Sector Economist, Food & Agri
thijs.geijer@ing.com

Maurice van Sante

Senior Economist Construction & Team Lead Sectors
maurice.van.sante@ing.com

Marcel Klok

Senior Economist, Netherlands
marcel.klok@ing.com

Paolo Pizzoli

Senior Economist, Italy, Greece
paolo.pizzoli@ing.com

Marieke Blom

Chief Economist and Global Head of Research

marieke.blom@ing.com

Raoul Leering

Senior Macro Economist

raoul.leering@ing.com

Maarten Leen

Head of Global IFRS9 ME Scenarios

maarten.leen@ing.com

Maureen Schuller

Head of Financials Sector Strategy

Maureen.Schuller@ing.com

Warren Patterson

Head of Commodities Strategy

Warren.Patterson@ing.com

Rafal Benecki

Chief Economist, Poland

rafal.benecki@ing.pl

Philippe Ledent

Senior Economist, Belgium, Luxembourg

philippe.ledent@ing.com

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

Inga Fechner

Senior Economist, Global Trade

inga.fechner@ing.de

Dimitry Fleming

Senior Data Analyst, Netherlands

Dimitry.Fleming@ing.com

Ciprian Dascalu

Chief Economist, Romania

+40 31 406 8990

ciprian.dascalu@ing.com

Muhammet Mercan

Chief Economist, Turkey

muhammet.mercan@ingbank.com.tr

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com

Sophie Freeman

Writer, Group Research

+44 20 7767 6209

Sophie.Freeman@uk.ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

James Knightley

Chief International Economist, US

james.knightley@ing.com

Tim Condon

Asia Chief Economist

+65 6232-6020

Martin van Vliet

Senior Interest Rate Strategist

+31 20 563 8801

martin.van.vliet@ing.com

Karol Pogorzelski

Senior Economist, Poland

Karol.Pogorzelski@ing.pl

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Viraj Patel

Foreign Exchange Strategist

+44 20 7767 6405

viraj.patel@ing.com

Owen Thomas

Global Head of Editorial Content

+44 (0) 207 767 5331

owen.thomas@ing.com

Bert Colijn

Chief Economist, Netherlands

bert.colijn@ing.com

Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

peter.vandenhoute@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Chris Turner

Global Head of Markets and Regional Head of Research for UK & CEE

chris.turner@ing.com

Gustavo Rangel

Chief Economist, LATAM

+1 646 424 6464

gustavo.rangel@ing.com

Carlo Cocuzzo

Economist, Digital Finance

+44 20 7767 5306

carlo.cocuzzo@ing.com