



R&R Weekly Column
By Brunello Rosa



Cracks Start To Emerge In The “Limitless” Friendship Between China and Russia

[Press reports](#) inspired by conversations with Chinese officials emerged last week, indicating that Russian officials were “increasingly frustrated” because China was not offering the type of support they had been expecting to receive from their powerful new ally. As a result, discussions between the two sides have been “tense” recently. In particular, China has reportedly not been offering the military support that Russia was looking for. This is somewhat confirmed by the words of the US secretary of state Antony Blinken, [who said that the US has not seen “a systematic effort” by China to help Russia](#) evade sanctions, nor any significant military support from China to Russia.

Theoretically, [China could buy some of Russia’s USD 130bn holdings of gold held by Russia’s central bank](#), and pay for it in US dollars. It could reactivate a currency swap line which was established after Russia’s annexation of Crimea in 2014, and it could serve as a lender of last resort to Russia. China could increase its purchases of natural resources from Russia (primarily oil, gas and industrial metals), or buy shares in some of Russia’s critical state-owned enterprises. China has in the past helped Iran to evade some of the US’ sanctions by using some of its smaller banks. [In our recent column](#), we said that China could offer, and likely has offered, Russia use of its international cross-border payment system (CIPS), instead of SWIFT, from which it has been banned by Western countries.

This bout of frustration for Russia may come as surprise news in the same weeks in which Russia and China, through the respective Foreign Ministers Wang Yi and Sergei Lavrov, [pledged to continue working together to establish “true democracy in the world, based on countries’ own conditions.”](#) This declaration of intent is the logical follow up to the solemn [joint statement made by Xi and Putin on February 4th](#), which began with the surprising sentence (for two autocratic leaders) that “democracy is a universal human value, rather than a privilege of a limited number of States, and that its promotion and protection is a common responsibility of the entire world community.” [There is clearly an attempt by Russia and China to re-define what democracy is.](#)

While these developments are obviously puzzling, we are not surprised by this apparent contradiction for several reasons.

First, China does not want to end up being caught by the US sanctions against Russia, which as usual carry a great deal of extraterritoriality. The US and Europe combined are still the destination for around 35% of Chinese exports, at a time when domestic growth in China is severely impacted by a) the lockdown imposed as a result of the zero-Covid policy; and b) the effects of the campaigns against tech companies, private education, and real estate developers, among others. So, China cannot really afford to substitute two of its largest trading partners with a small and declining economy such as Russia.

Second, we have already [questioned the rationality of Xi’s decision to choose Russia](#) as its ally in Cold War II against the US, considering how unpredictable Putin is, especially if he really is being [affected by serious diseases, as some reports suggest](#). Unsurprisingly, [now reports are starting to be published questioning Xi’s physical and mental health](#), and his fitness for the top job. They are published by Chinese sources, however credible, living abroad and anonymously republished in mainland China.

Third, we must take into account the ongoing power struggle in China ahead of this autumn’s congress of the Chinese Communist Party, which will choose the Party’s official leadership, with Xi running for a third mandate in the first official step of establishing himself as leader of the country for life. If this happens, this would mark the interruption of the mechanism adopted since the 1980s to choose the country’s leader, in which the president and prime minister serve only two five-year terms (with the prime minister then touted to succeed the president at the end of his second mandate). [Numerous reports suggest that Premier Li Keqiang could be getting ready to succeed Xi later this year](#), by capitalising on the widespread discontent caused by Xi’s anti-graft and Zero-Covid campaigns, which have - according to Li - greatly damaged the economy (which he is officially responsible for). So, Xi needs to show that his choices are still rational and not dictated by the needs of Putin, whose judgment abilities may be compromised.

All this suggests that the first cracks may start emerging in the new alliance between China and Russia, which was in effect supposed to be limitless. The front of the two autocracies within the UN Security Council may not be as united as Xi purported it was when he called US President Biden [to congratulate him for his victory in 2020](#). On that occasion, Xi reportedly told Biden that “autocracies, not democracies, will run the world in coming decades,” as in an increasingly complex world in rapid evolution, quick responses were needed. But “democracies require consensus and consensus takes time to build, but countries have no time.” When reporting on the content of his conversation with Xi, Biden concluded that Xi was “wrong.” Perhaps these recent tensions between China and Russia prove that democracies will be able to survive as an effective way of governing for a bit longer

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Looking Ahead

The Week Ahead: US Core Inflation To Cool Down a Bit; UK PMIs To Fall; ECB To Keep Rates Unchanged in June

In the US, in May, inflation is expected to stay unchanged at 8.3% y-o-y, whereas core inflation is likely to slow down to 5.9% y-o-y (*p*: 6.2%). In June, Michigan Consumer Sentiment is likely to edge down to 58.1 (*p*: 58.4).

In the EZ, according to a third estimate, in Q1, GDP is expected to advance by 0.3% q-o-q (*p*: 0.3%) and 5.1 % y-o-y (*p*: 4.7%).

Still in the EZ, the ECB is expected to keep its policy stance unchanged with the main refi rate at 0%, the depo rate at -0.5% and the marginal refinancing rate at 0.25%. The ECB is expected to pave the way for a rate liftoff in July.

In the UK, the final data for S&P Global/CIPS in May is expected to show that: *i*) services PMI falls to 51.9 (*p*: 58.9); and *ii*) composite PMI decreases to 51.8 (*p*: 58.2)

The Quarter Ahead: UK To Place New Safeguards For Stablecoins; Ukraine War Enters Its 100th Day

The U.K. Government proposed an insolvency regime to manage the failure of major crypto stablecoin. Stablecoins are crypto-assets that are pegged to traditional assets such as the US dollar. The collapse of the Terra-Luna trade has intensified concerns over the global crypto market. Under the plan proposed by the UK Treasury, the Bank of England would gain new powers to take over collapsed stablecoins. By placing special oversight over stablecoin issuers, the Bank of England would ensure to protect consumers if stablecoins fail. The Treasury is also planning to make stablecoin a legal form of payment with an aim of making Britain a 'crypto hub'.

Ukraine war enters its 100th day and Russia controls 20% of the territory. The UK's Ministry of Defense reports that Russia controls more than 90% of the Luhansk region. On the other hand, Ukraine has some success in the battles in Sievierodonetsk, in eastern Ukraine. Contrary to disinformation spread by Russia, Ukraine does not intend to use weapons provided by the U.S. to attack Russian territory

Last Week's Review

Real Economy: US Unemployment Stayed Unchanged; EZ Inflation Accelerated; PMIs Declined In Developed Markets

In the US, May's unemployment rate stayed unchanged at 3.6% (*c*: 3.5%; *p*: 3.6%). The US economy added 390K jobs (*c*: 325K; *p*: 436K) better than expected despite concerns over an economic slowdown. However, NFP posted the smallest gain since April 2021.

In the EZ, according to flash estimates, May's inflation data showed that: *i*) CPI inflation rose to 8.1% y-o-y (*c*: 7.7%; *p*: 7.4%); and *ii*) core inflation increased to 3.8% y-o-y (*c*: 3.5%; *p*: 3.5%). April's unemployment rate stayed unchanged at 7.8% as expected. May's consumer confidence stayed unchanged at -21.1 (*p*: -22). In April, retail sales accelerated to 3.9% y-o-y (*c*: 5.4%; *p*: 1.6%), whereas shrank on a monthly basis to -1.3% (*c*: 0.3%; *p*: 0.3%).

In DMs, in May, final PMIs softened as: *i*) EZ manufacturing and services (*p*: 57.7) slowed down to 54.6 (*c*: 54.4; *p*: 55.5) and 56.1 (*c*: 56.3; *p*: 57.7) respectively and as a result composite PMI decreased to 54.8 (*c*: 54.9; *p*: 55.8); *ii*) UK's manufacturing indicator fell to 54.6 as expected (*p*: 55.8); *iii*) US manufacturing and services slowed down to 57 (*c*: 57.5; *p*: 59.2) and 53.4 (*c*: 53.5; *p*: 55.6) respectively and as a result of which composite PMI is down too to 53.6 (*c*: 53.8; *p*: 56.0); and *iv*) Japan's manufacturing was slightly down to 53.3 (*c*: 53.2; *p*: 53.5), whereas services PMIs accelerated to 52.6 (*c*: 51.7; *p*: 50.7).

In Canada, the Bank of Canada raised the target for its overnight rate by 50bps to 1.50%.

Financial Markets: Stock Markets Are Down; Yields Rose; Dollar Index Extended Its Gains; Oil Was Up and Gold Down

Market Drivers: Investors continue to question the real feasibility of an economic 'soft landing'. Following stronger-than-expected U.S. jobs data, expectations for tightening monetary policy were reinforced and, as a result, U.S. yields rose substantially.

Global Equities: Decreased *w-o-w* (MSCI ACWI, -0.6%, to 649.2). The US S&P 500 index fell (-1.2% *w-o-w*, to 4,109), marking the eighth decline in past nine weeks. The EZ, shares were down (Eurostoxx 50, -0.7% *w-o-w*, to 3,783.7), as investors digested EU announcement of a partial ban on Russian oil imports and disappointing monthly retail sales. In EMs, equities rose (MSCI EMs, +1.7%, to 1,061). Volatility rose to 26.0 (VIX S&P 500, 52w avg.: 22.3; 10y avg.: 18.1).

Fixed Income: *w-o-w*, 10-year US treasury yields increased (+20 bps to 2.94%). The 2-year US Treasury yields were up too (+17 bps to 2.66%). German 10-year bund yield increased (+30 bps to 1.26%).

FX: *w-o-w*, the US Dollar Index was up (DXY, +0.5%, to 102.2; EUR/USD -0.1%, to 1.07). In EMs, currencies strengthened (MSCI EM Currency Index, +0.3% *w-o-w*, to 1,699.14).

Commodities: *w-o-w*, oil prices rose (Brent, 1.4% to 121.1 USD/b) in the week in which OPEC+ agreed to increase production targets by more than planned, but failed to exclude Russia from the increase. Gold prices fell *w-o-w* (-0.2% to 1,853.9 USD/Oz).



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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	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