



R&R Weekly Column
By Brunello Rosa



The EU's Ruling Coalition Might Need Support From Populist Parties To Reach A Majority

Last week, when we [commented on the selection of the new heads](#) of the top five EU institutions, we highlighted how the end of the musical chairs game that the selection process resembled [delivered only a very a fragile political equilibrium](#). We also took a non-consensus view of the situation, arguing that time is on the side of the national-populist parties in Europe, which, during the five-year tenure of this new parliament, will have the option of making a proposal to the European People's Party (EPP) to form a coalition together. Already during the past week, events of this kind have been unfolding more rapidly than even we would have expected.

As [numerous press reports suggest](#), the new EU Commission (EC) President Ursula Von Der Leyen is having a hard time securing the votes she will need on July 16th if she wants to win a vote of confidence from the EU Parliament. With the far-left GUE and the Greens having formally announced their vote of no confidence towards President Von Der Leyen, she now needs to rely on a three-party coalition of EPP (179 seats), Socialists & Democrats (153 seats) and Liberals (105 seats). Theoretically speaking, this ruling coalition could count on 437 votes, much more than the 374 necessary to reach a majority in the 750-seat European Parliament.

However, a number of MEPs, especially those from the German Social Democrats, are still upset by the method by which Von Der Leyen was chosen (in particular, the trashing by French President Macron and German Chancellor Merkel of the *Spitzenkandidat* system that was introduced in 2014). Others are unimpressed by the lack of ambition of her political program, which so far seems to be just a sensible continuation of the status quo. Additionally, some members of the EPP, such as Viktor Orbán's Fidesz, want a softer stance taken by the future EC regarding the application of Article 7 (namely, the sanction imposed on misbehaving countries) in exchange for their vote. So, what seemed to be a vote that Von Der Leyen could take for granted could instead become extremely problematic.

Facing this situation, it was suggested to her to postpone the vote to September, so that she could gain more time to convince the rebellious MEPs to give her their support. But she understood that nothing would change in the next two months, and that her position could become even weaker if she were to let this situation fester for a longer period of time.


But here is where the situation becomes intriguing, if perhaps also dangerous. A number of populist-nationalist parties have offered their support to Von Der Leyen, in exchange for a more favourable attitude taken by the EC President on the dossiers close to the various party leaders. PiS, the Polish party of the nationalistic leader Jarosław Kaczyński, has offered its support in exchange for a softer stance on the application of Article 7, like Hungary's Fidesz. Lega and Five Star have offered their votes in return for a "heavy" portfolio for Italy in the new EC, such as Competition, or Industry.

Von Der Leyen might manage to convince the rebellious MEPs from her own coalition to fall into line and allow the Commission to have a working and cohesive majority from the start of her term. But she might not have enough time for that. In that case, she may be forced to accept parties to allow for the birth of a Commission presided over by herself. Such a Commission would become vulnerable to the requests of the national-populists sooner than even we had anticipated. Von Der Leyen's manoeuvring space to reform Europe in the direction of the "United States of Europe" (the way she reportedly would like to see the EU become) would be further reduced. As a result, the process of EU dis-integration would likely accelerate further in coming years.


If Von Der Leyen fails to reach a majority this week, this would open up a serious institutional crisis in the EU, forcing EU leaders to find another solution. Such a solution is difficult to identify, as Von Der Leyen was chosen as part of a "package" that is difficult to unbundle, a package which also included the selection of David Sassoli who has been already elected President of the EP, Charles Michel as President of the EU Council, and the arrival (which [markets have already greeted positively](#)) of Christine Lagarde at the helm of the ECB.

Our Recent Publications

 [Brexit and BoE Update: Brace For Political Turmoil In Coming Months](#), by Brunello Rosa and Nouriel Roubini, 12 July 2019

 [FRANCE: Macron's Push For French and European Reform Remains, But Will Be Constrained](#), by Brunello Rosa and Nouriel Roubini, 9 July 2019

 [Flash Review: Bank of Canada Now On Hold, Ready To Go Either Way](#), by Brunello Rosa, 10 July 2019

 [Geopolitical Corner: Will Ramaphosa Deliver South Africa's Economic Promise?](#), by John C. Hulsman, 2 July 2019

Looking Ahead

The Week Ahead: Economic Activity Slows And Growth Decelerates

In the US, economic activity is likely to have slowed down (IP Jun., c: 0.2% m-o-m; p: 0.4; Retail sales, c: 0.3% m-o-m; p: 0.5).

In China, Q2 growth is expected to have decelerated (GDP, c: 6.2% y-o-y; p: 6.4) as economic activity remains sluggish (IP Jun., c: 5.2% y-o-y; p: 5.0; Retail sales Jun., c: 8.3% y-o-y; p: 8.6).

In the EZ, inflation is expected to remain unchanged (CPI Jun., c: 1.2% y-o-y; p: 1.2; core CPI, c: 0.8; p: 1.1).

In Japan, inflation is likely to rise but remain below target (National CPI Jun., c: 0.8% y-o-y; p: 0.7; National core CPI, c: 0.6%; p: 0.5).

The Quarter Ahead: Risks To Global Trade To Remain

In the US, the Trump admin. is set to investigate French plans to tax US technology giants, e.g.: Facebook and Amazon, over concerns that “the move unfairly targets American companies” – reiterating the same rhetoric that brought the US to impose tariffs on China.

In the US, Fed Chair Jerome Powell provided further hints about an impending rate cut. Despite strong-than-expected hiring in the US, Powell pointed at: *i)* low inflation in the Fed’s preferred inflation gauge, the PCE, due to slow wage growth; and *ii)* economic data showing that “manufacturing, trade, and investment are weak all around the world”. Ahead of the Fed’s July meeting, the market expectations of: *i)* “two rate cuts” rose to 22.5% (p: 5.4); and *ii)* “one rate cut” fell to 77.5% (p: 94.6).

In the EZ, the EC cut its inflation outlook for 2019 and 2020 to 1.3% (p: 1.4). The ECB June meeting minutes revealed the CB’s inclination to inject fresh stimulus via: *i)* interest-rate cuts; and/or re-starting net asset purchases.

In the UK, Chancellor Phillip Hammond said that he would back a legal challenge against the government if the new Prime Minister tried to suspend parliament – in order to “force through a no-deal exit”.

In China, the PBoC is expected to accelerate “reforms to simplify the policy rate transmission”, as the CB governor hinted at plans to scrap the benchmark lending rate, while keeping the deposit rate to reduce borrowing costs for companies and lift domestic demand.

In Turkey, after the delivery of the first shipment of the Russian S-400 system, the Trump administration will monitor developments - following earlier threats to punish Turkey by imposing sanctions over the purchases.

Last Week’s Review

Real Economy: Geopolitical Risks And Subdued Inflation Support CB Easing

In the EZ, industrial production remains sluggish (a: -0.5% y-o-y; c: -1.6; p: -0.4), as German industrial activity continues to weaken (IP, a: -3.7% y-o-y; c: -1.1; p: -2.3).

In China, trade weakened in June (Exports, a: -1.3% y-o-y; c: -2.0; p: 1.1; Imports, a: -7.3% y-o-y; c: -4.5; p: -8.5), due to: *i)* the tariff-tensions between the US and China; *ii)* sluggish domestic demand; and *iii)* weaker commodity prices. Inflation remains muted (CPI Jun., a: 2.7% y-o-y; c: 2.7; p: 2.7).

In Japan, industrial production slowed further (a: -2.1% y-o-y; c: -1.8; p: -1.8).

In Iran, the UK Navy intervened to allow a BP Plc-operated oil tanker, blocked by Iranian vessels, to leave the Persian Gulf.

In Singapore, the economy - open and trade-reliant - unexpectedly contracted (Q2 GDP, a: -3.4% q-o-q; c: 0.1; p: 3.8), as trade tensions weakened business confidence and activity. Inflation remains subdued. In the US, core inflation came in slightly above expectations in June (core CPI, a: 2.1% y-o-y; c: 2.0; p: 2.0); however the broader inflation measure declined (CPI, a: 1.6% y-o-y; c: 1.6; p: 1.8).

Financial Markets: Weak Economic Data Support Expectations Of Future CB Easing, Lifting The Markets

Market drivers: As Fed’s Powell all-but-confirmed a rate-cut in the July meeting, investors sought risky assets, in particular US equities.

Stocks: w-o-w, global stocks rose (MSCI ACWI, +0.2%). Volatility fell (VIX S&P 500, -0.9 points to 12.4, 52w avg.: 16.4; 10y avg.: 17.2). US equities hit a record-high (S&P 500, +0.8%) and EZ stocks fell (Eurostoxx, -0.9%).

Bonds: w-o-w, globally, indices declined (BAML Global bond index, -0.4%). A search for yield is driving investors to Italian bonds (10Y Italian bond, -1 bps to 1.73%). The country received EUR 17bn in orders at an offering of EUR 3bn of an existing 50-year security maturing in 2067.

FX: the USD depreciated (DXY, -1.5%) against a basket of currencies and EM FX remained flat (MSCI EMs, +0.2% at 1,651).

Commodities: Oil prices rose w-o-w, after: *i)* US Government data showed a larger-than-expected drop in stockpiles; *ii)* escalation of tensions in the Persian Gulf; and *iii)* a storm in the Gulf of Mexico (Brent, +3.9% to 66.7 USD/b).



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The picture in the front page comes from [this website](#)



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



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