



R&R Weekly Column
By Brunello Rosa



Inequality As A Cause Of The “Populist International”

We have written several times about [the rise of populism at global level](#), and its repercussion on the political, economic, and financial developments of the countries in which the populist phenomenon is strongest. We have also discussed the [potential repercussions for the liberal order](#) and its institutions, [such as the European Union](#), that were created after World War II as a response to the damage caused by the nationalistic and populist movements of the first half of the 20th century.

Plenty of studies have been published that discuss the origin of this new wave of populism. [A useful taxonomy](#) is one in which contemporary populists have been classified into three categories: those who reached power for cultural or “identity-related” reasons (e.g. [Brexit](#)); those who claim to be anti-establishment (e.g. [Donald Trump](#)), and finally, those who came to power as a result of a widespread socio-economic malaise (e.g. [Five Star and Lega in Italy](#)). In this column we want to focus on the underlying causes of the last of these three categories: *socio-economic populism*. At the core of any economic malaise there is under-development and lack of opportunity, [especially in emerging markets](#). In developed economies, however, where per capita income is much higher, it is the uneven or unfair distribution of income and wealth that seems to be the driving force behind the rise of populist forces in recent years.

As discussed in [our recent in-depth analysis](#), income and wealth inequality ([or lack of “inclusion”, to use the expression of the IMF/World Bank](#)) is one of the main causes of subdued growth and historically low real interest rates. As the IMF said in its 2018 Annual Report, “[reducing inequality can open doors to growth and stability](#).” Yet by causing subdued and uneven growth, inequality is also a primary origin of protest movements that want to rectify this situation, which sometimes are or have been classified as “populist.”


In our analysis we discuss how income inequality has been increasing since the 1970s, when the primary distribution of income began to become skewed more towards profits, interests and rents and less to labour. At the same time, the *neo-liberist* revolution of Ronald Reagan and Margaret Thatcher also made the redistribution of income via taxation and subsidies less effective, on the back of what was labelled as *trickle-down economics*. Many years of increased globalisation, with its inherently deflationary forces (including on wages), reduced labour share of income in the most advanced economies (and parallel increase in the profit and interest share of income), diminished power of trade unions, mass privatisation of public goods, and inability of taxation and subsidies to redistribute income in a fairer way, have led to the current situation. Workers in many countries feel deprived, and are therefore willing to give a chance to political leaders who claim to be on their side, however inconsistent with this claim those leaders’ biographies might be.


The policy solution to this problem seems quite straightforward: a more active role of fiscal policy, to promote income redistribution, increased public expenditure in infrastructure and education, the [provision of job opportunities to younger generations](#) by the public and private sectors. Some of these solutions are becoming popular even among the US electorate, with the rise of political leaders such as Bernie Sanders and Alexandria Ocasio-Cortez, who are not afraid of being labelled “socialists,” a description which just a few years ago would have killed any political career. Nevertheless these solutions are easier said than done. Once in power, even their proponents realise how difficult implementing such policies tends to be, given binding budget constraints.


Wealth inequality is even harder to assess than is income inequality, as it is often a legacy issue (as wealth is accumulated over generations), and as it is the result of the cumulative effect of income inequality over a long period of time. A group of economists has suggested the adoption [of a “wealth tax” as a solution to this issue](#). This might well be a solution, but the political economy of adopting such a tax would be complicated, and so might ultimately prove to be counter-productive.

All this is to say that income and wealth inequality are here to stay for the time being, and will continue to feed populist movements around the globe. Policy solutions are available, but their implementation is complicated and sometimes politically toxic. This means that probably things will have to get worse before they can get better.

Our Recent Publications

 [Scenario Analysis: Tensions Between Iran And US Likely To Continue, With Increasing Risk Of Escalation](#), by Giorgio Cafiero, Nouriel Roubini and Brunello Rosa, 14 August 2019

 [Income and Wealth Inequality Continues to weigh on global growth](#), by Francesca Panelli, 16 August 2019

 [GEOPOLITICAL CORNER: India Lights The Kashmiri Powder-Keg](#), by John Hulsman, 13 August 2019.

Looking Ahead

The Week Ahead: In The EZ Manufacturing Weakens And FED Soon To Announce Future Movements

In the EZ, manufacturing sector activity is expected to weaken (Markit Manuf. PMI Aug., c: 46.3; p: 46.5), led by a sluggish industrial activity in Germany (Markit Manuf. PMI, c: 43.0; p: 43.2); yet, PMI indicators in the services sector are likely to remain expansionary (c: 52.7; p: 53.2). Inflation is expected to slow (CPI Jul., c: 1.1% y-o-y; p: 1.3; Core CPI, c: 0.9% y-o-y; p: 1.1).

In the US, Chairman Powell will deliver a speech at the Fed's Jackson Hole symposium on Aug 23; the markets will focus on whether the Fed's is planning: *i*) a long-term cutting cycle, against a global recession; or *ii*) a few insurance cuts, against an economic downturn.

The Quarter Ahead: Geopolitical Tensions Will Remain High and Central Banks Are Ready to Ease Policy

In the US, President Trump announced the delay tariffs on Chinese imports "until December to shield US consumers during the Christmas shopping season"; however, some goods such as clothing, watches, and electronics will face levies of 10% starting September 1. Overall, 69% of Chinese consumer goods will be subject to tariffs by September 1, up from the current 29%. Although economic data indicate: *i*) resilience in manufacturing and services; and, *ii*) a pick-up in inflation - market expectations for "one rate cut" at the Fed's September meeting remain high, at 78.8% (p: 84.6), due to rising concerns over trade and weaker global conditions.

In the UK, PM Johnson will reiterate at the upcoming G7 summit in France that the British parliament "will not, and cannot, cancel the referendum".

In the EZ, to support the flagging EZ economy amid trade uncertainties, according Governing Council member Olli Rehn the ECB is "preparing a 'very strong package' of stimulus measures that should exceed investors' expectations", to be announced at the September policy meeting.

In China, the PBoC is set to replace the key lending rate with a market-driven benchmark - aimed at lowering borrowing costs for companies that have faced: *i*) tighter access to credit; and *ii*) poor investor sentiment, caused by the ongoing trade war.

Last Week's Review

Real Economy: Weak Economic Data Point To A Global Downturn

In the US, retail sales rose unexpectedly in July (a: 0.7% m-o-m; c: 0.3; p: 0.3), indicating that personal consumption—about 70% of US GDP—remains strong. Inflation rose more than expected in July (CPI, a: 1.8% y-o-y; c: 1.7; p: 1.6; Core CPI, a: 2.2% y-o-y; c: 2.1; p: 2.1) as tariffs begin to impact prices.

In the EZ, growth stagnated (GDP Q2; a: 0.2% q-o-q; c: 0.2; p: 0.2), as: *i*) IP weakened more than expected (a: -2.6% y-o-y; c: -1.2; p: -0.8); and *ii*) Germany - the largest economy - contracted in Q2 (a: -0.1% q-o-q; c: -0.1; p: 0.4). Investor sentiment on Germany's economic outlook fell to the lowest since 2011 (ZEW economic sentiment survey, a: -43.6; c: -21.7; p: -20.3).

In Japan, manufacturing keeps contracting, albeit at a slower pace (IP Jun., a: -3.3% y-o-y; c: -3.6; p: -3.6).

In the UK, inflation accelerated faster-than-expected (CPI Jul., a: 2.1% y-o-y; c: 1.9; p: 2.0).

In China, economic activity continued to slow down, as in July: *i*) retail sales softened (a: 7.6% y-o-y; c: 8.6; p: 9.8); and, *ii*) industrial activity weakened (IP, a: 4.8% y-o-y; c: 5.8; p: 6.3).

In Turkey, industrial output fell for a 10-month running (IP Jun., a: -3.9% y-o-y; c: -1.0; p: -1.3).

In Argentina, Fitch downgraded the country's credit rating to CCC (p: B).

In Mexico, BdeM cut its interest rate (a: 8.00%; c: 8.25; p: 8.25).

Financial Markets: Risk-Off Sentiment Driven By Trade-Related Uncertainties And EM Volatility

Market drivers: indicators pointing to a global downturn and persistent trade uncertainties drove investors to safe-haven assets.

Stocks: w-o-w, global stocks fell (MSCI ACWI, -1.2%) driven by both the US (S&P500, -1.3% to 2,889) and EMs (MSCI EMs, -1.1% to 970). Volatility rose (VIX S&P 500, +4.4 points to 18.5, 52w avg.: 16.7; 10y avg.: 17.1).

Bonds: w-o-w, global indices rose (BAML Global bond index, +0.9%). The 10y UST yield fell w-o-w by 19 bps, to 1.54%. In MENA, bond supply stands at USD 67.0bn y-t-d, compared to USD53.2bn in 2018.

FX: the USD appreciated (DXY, +0.7%) against a basket of currencies. The EUR fell (EUR/USD, -1.0% to 1.109). EM FX fell (MSCI EMs, -0.3% at 1,607), bar the Chinese Renminbi (USD/CNY, +0.3% to 7.041). In Argentina, the incumbent President's defeat in the primary elections led to a Peso sell-off (USD/ARS, -17.5% to 52.834).

Commodities: Oil prices rose (Brent, 0.2% to 68.6 USD/b). Gold rose (1.1% to 1,514 USD/Oz.).

Farah Aladsani contributed to this Viewsletter.

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



@RosaRoubini



Rosa & Roubini



Rosa&Roubini Associates

For more information, please call us on +44 (0)207 1010 718 or send us an email to info@rosa-roubini-associates.com

www.rosa-roubini-associates.com

118 Pall Mall, London SW1Y 5ED



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



Rosa & Roubini Associates Ltd is a private limited company registered in England and Wales (Registration number: 10975116) with registered office at 118 Pall Mall, St. James's, London SW1Y 5ED, United Kingdom. VAT registration number GB 278 7297 39. **Analyst Certification:** We, Brunello Rosa and Nouriel Roubini, hereby certify that all the views expressed in this report reflect our personal opinion, which has not been influenced by considerations of Rosa & Roubini Associates's business, nor by personal or client relationships. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the views expressed in this report. **Disclaimer:** All material presented in this report is provided by Rosa & Roubini Associates-Limited for informational purposes only and is not to be used or considered as an offer or a solicitation to sell or to buy, or subscribe for securities, investment products or other financial instruments. Rosa & Roubini Associates Limited does not conduct "investment research" as defined in the FCA Conduct of Business Sourcebook (COBS) section 12 nor does it provide "advice about securities" as defined in the Regulation of Investment Advisors by the U.S. SEC. Rosa & Roubini Associates Limited is not regulated by the FCA, SEC or by any other regulatory body. Nothing in this report shall be deemed to constitute financial or other professional advice in any way, and under no circumstances shall we be liable for any direct or indirect losses, costs or expenses nor for any loss of profit that results from the content of this report or any material in it or website links or references embedded within it. The price and value of financial instruments, securities and investment products referred to in this research and the income from them may fluctuate. Past performance and forecasts should not be treated as a reliable guide of future performance or results; future returns are not guaranteed; and a loss of original capital may occur. This research is based on current public information that Rosa & Roubini Associates considers reliable, but we do not represent it is accurate or complete, and it should not be relied on as such. Rosa & Roubini Associates, its contributors, partners and employees make no representation about the completeness or accuracy of the data, calculations, information or opinions contained in this report. Rosa & Roubini Associates has an internal policy designed to minimize the risk of receiving or misusing confidential or potentially material non-public information. We seek to update our research as appropriate, but the large majority of reports are published at irregular intervals as appropriate in the author's judgment. The information, opinions, estimates and forecasts contained herein are as of the date hereof and may be changed without prior notification. This research is for our clients only and is disseminated and available to all clients simultaneously through electronic publication. Rosa & Roubini Associates is not responsible for the redistribution of our research by third party aggregators. This report is not directed to you if Rosa & Roubini Associates is barred from doing so in your jurisdiction. This report and its content cannot be copied, redistributed or reproduced in part or whole without Rosa & Roubini Associates' written permission.

