



R&R Weekly Column
By Brunello Rosa



A Compromise Is Struggling to Emerge At The Crucial EU Summit

Since last Friday, the [special EU summit](#) to decide on the implementation of the [Recovery and Resilience Facility](#) is taking place in Brussels, with European leaders meeting in person for the first time after months of video conferences.





The summit started with a great distance between the positions of the so-called Frugal Four (Austria, Netherlands, Denmark and Sweden) – which became Frugal Five when Finland joined the group – and those of the Mediterranean front of Italy and Spain (which is supported by France). The former group wants a reduction of the overall package proposed by the EU Commission, namely EUR 500bn in transfers and EUR 250bn in loans, and a significant reduction in the amount made up by transfers. Within this group, the most aggressive position is expressed by the Netherlands, whose PM Mark Rutte seeks to win a majority in his country's parliamentary election next spring. The Netherlands, for a change, is not simply the “bad cop” of the duo with Germany. Rather, the two countries entered this meeting with two different strategic objectives. The second group of countries wants the overall size of the program to be left unchanged, and wants transfers to remain the bulk of it.

There is also a third front at the table, representing the nations of the so-called Visegrad group (Czechia, Slovakia, Hungary and Poland). Those countries, among the largest beneficiaries of EU funds (Poland in particular) want to make sure that their quota of funds in the new Multiannual Financial Framework (MFF) remains intact. Alliances across regions (North/South, East/West) and political families (People's party, Socialists and Democrats, Liberals) are variable, and [subject to change opportunistically](#).

In the middle of these different positions is Germany, with Angela Merkel trying to broker a historic deal during the period in which Germany holds the rotating EU presidency, to make sure that the eventual result is acceptable to everybody. [Germany is doubly putting its face on this deal](#). The EU Commission that made the initial proposal discussed at the summit is led by Ursula Von der Leyen, the former German defence minister and protégé of Angela Merkel. In addition, Merkel herself is looking to complete her long period in service with an agreement that could prove historical. [Merkel's goal is passing the EU to the next generation of European leaders](#), with some of the elements of solidarity that characterised the initial project still intact. So, Germany cannot risk that this summit ends with no results.

Given such distance between the positions of various blocs of countries to begin with, the sessions on Friday, Saturday and Sunday not surprisingly finished in acrimonious discord. Various proposals have been presented by EU Council President Charles Michel to reduce the overall size of the package and the share of that package made up by transfers rather than loans, to make the deal more acceptable to the Frugal Five. The latest proposal foresees EUR 390bn of grants and will be discussed starting from Monday afternoon. We expect that, eventually, a compromise will emerge, if not at this meeting, at a new one later in July.

Our Recent Publications

-  [Flash Reviews: ECB Takes Stock Of The Stimulus Provided Since March](#), by Brunello Rosa and Farah Aladsani, 16 July 2020
-  [Flash Review: BOJ Remains On Hold But Ready to Act](#), by Brunello Rosa and Fawaz Sulaiman Al Mughrabi, 15 July 2020
-  [Flash Review: BOC Remains On Hold But Introduces Forward Guidance](#), by Brunello Rosa, 15 July 2020
-  **GEOPOLITICAL CORNER:** [The Anglosphere Rides Again, This Time Uniting Around an Anti-Chinese Geo-Strategy](#), by John Hulsman, 14 July 2020

Looking Ahead

The Week Ahead: PMIs Are Expected To Vary Significantly

In DMs, manufacturing PMIs are expected to vary significantly, with: *i)* US indicators pointing to a recovery (c: 51.3; p: 49.8); and *ii)* Japan figures deteriorating (c: 39.5; p: 40.1). Across DMs, services PMIs are likely to recover (US, c: 50.2; p: 47.9; EZ, c: 51.0; p: 48.3).

The Quarter Ahead: Geopolitical Tensions To Hamper Global Supply Chains, While Security Risks Emerge Over Vaccine Development

US-China tensions are likely to remain high. In a letter addressed to a group of global CEOs, President Xi Jinping pledged to provide ‘a better business environment for foreign firms’. Meanwhile, President Trump reiterated calls for American and other foreign companies “to rewire and shorten their supply chains”.

In the US, a tough stance on China is garnering bipartisan support: the current presidential frontrunner, Mr. Joe Biden, holds a similar policy stance on Beijing and supply chains, including plans to: *i)* use ‘targeted restrictions on imports from nations such as China that pose national security threats’; and, more broadly, *ii)* impose that technology that is developed in the US is also manufacturing there.

The EC President, Mr. Charles Michel, offered a compromise solution for the EUR 750bn recovery fund - in an attempt to overcome structural disagreements on how disbursements will be governed. The deadlock was led by the Dutch PM, Mr. Mark Rutte, who insisted on the right to ‘unilaterally veto payments’ to countries that do not meet reform demands. The revised plan includes: *i)* the ability for any single country to object to payouts to a member state—but only ‘if done within a three-day window’ –; *ii)* shifting EUR 50bn from grants to loans; and *iii)* an additional budget rebate to the ‘frugal-four states’ – i.e., the Netherlands, Austria, Denmark and Sweden. While Mr. Rutte, the leading opposer, said that the new proposal was a ‘step in the right direction’, the ‘frugal-four’ reiterated their calls for deeper cuts to the overall size of the package.

The US, UK and Canada blamed a state-backed Russian hacking group for cyber espionage against institutions involved in COVID-19 vaccine development. Efforts to develop a vaccine turned into a race, where winners are set to exponentially benefit from access to treatments.

Last Week's Review

Real Economy: US Job Recovery Slows, Geopolitical Risks Rise, Central Banks Remained Accommodative

In the US, weekly initial jobless claims recorded their smallest decline since March (a: 1.30m; p: 1.25m; c: 1.31m), suggesting that the job-recovery has entered a slower phase. Yet, June retail sales rose by 7.5% m-o-m (p: 18.2); the increase: *i)* exceeded expectations of a 5.0% rise; and *ii)* lifted the overall level of retail sales to just 1.0% under its pre-pandemic peak. IP also rose (a: 5.4% m-o-m; c: 4.3; p: 1.4) but remained well below its pre-pandemic levels (a: -10.8 y-o-y; p: -15.4), as damaged supply chains take longer than consumption to benefit from eased lockdowns.

In the UK, the recovery will be slower than initially anticipated: in May the economy posted a weaker-than-expected output rebound: 1.8% m-o-m (c: 5.5; p: -20.3).

In China, in Q2, GDP grew by 11.5% q-o-q (c: 9.6; p: -10.0); however economic data showed: *i)* recovery in the industrial sector (IP, a: 4.8% y-o-y; c: 4.8; p: 4.4; fixed asset investment, a: -3.1% y-o-y; c: -3.3; p: -6.3); and *ii)* continued weakness in consumption (retail sales, -1.8% y-o-y; c: 0.3; p: -2.8).

In the US, June's CPI inflation rose for the first time in four months on the back of higher energy and food prices (a: 0.6% y-o-y; c: 0.6; p: 0.1); however, underlying core inflation remained flat at 1.2% y-o-y (c: 1.1).

In the EZ, Japan, and Canada, Central banks made no major policy changes and reiterated their commitment to keep: *i)* interest rates low; and *ii)* asset purchases in place - until the economic recovery is underway.

Financial Markets: CB Liquidity And Vaccine-Related Optimism Supported Market Sentiment

Market drivers: hopes for a COVID-19 vaccine continued to override data-based concerns of a slow, prolonged global recovery.

Equities: w-o-w, global stocks rose (MSCI ACWI, +1.2%, to 548), driven by the US (S&P 500, +1.2%, to 3,225) and EZ (Eurostoxx 50, +2.1% to 3,366). EM equities fell (MSCI EMs, -1.3%, to 1,055), led by Chinese equities (Shanghai Comp., -5.0% to 3,214).

Fixed income: w-o-w, global debt indices were flat (BAML Global, +0.1% to 296.9), as were yields across DMs (10y UST, -1bps to 0.63%; 10y German Bunds, +2 bps to -0.45%).

FX: w-o-w, the USD weakened against a basket of currencies (DXY, -0.7% to 95.942). The EUR strengthened after an initial positive reception of the draft EU recovery fund proposal (EUR/USD, +1.1% to 1.143).

Commodities: Oil prices remained flat (Brent, -0.2% to 43.1 USD/b). Gold maintained its haven appeal (Gold, +0.6% to 1,809 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



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