

MAKING SENSE OF *THIS* WORLD

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By Brunello Rosa



Economic, Tech And Geopolitical Events Further Complicate The US Presidential Race

Last week, the US Bureau of Economic Analysis released its first estimate of the performance of the US economy in Q2 2020. After the 5% q/q drop in Q1 (a seasonally-adjusted annualised rate, SAAR), in Q2 the economy contracted by 32.9% q/q SAAR. This was slightly less than anticipated (34.1%), but still the largest contraction on record. This quarterly contraction of 8-9% (32.9% divided by four) is in line with the fall in income recorded by other major economies. It is explained, of course, by the adoption of lockdown measures that were introduced in order to slow down the spread of Covid-19.

As the Federal Reserve Chairman Jerome Powell said during the press conference following the FOMC decision to leave the central bank's policy stance unchanged in July, this is the largest shock the US has had to endure in recent history. After an unexpected rebound in May and June, the recovery of economic activity since July has slowed down, as has been revealed by non-standard, high-frequency indicators, such as hotel occupancy and credit card use. In its latest statement, the Federal Reserve decided to establish a clear link between the expected path of economic activity and the likely evolution of the pandemic.

Following the release of the quarterly GDP figures, US President Donald Trump released a tweet in which he wondered whether the US election could be delayed "until people can vote properly, securely and safely." Even if it is not in the president's power to decide on the date of the election, this tweet created an outcry in the media and the Democratic party, where it was often viewed as a confirmation of Trump's authoritarian tendencies and an attempt to undercut the US democracy. Since the power to postpone the date of the election has resided with Congress since 1845, Trump's tweet must be read as a signal of how he is ready to contest any result that would not see him as the victor in the US presidential race in November, as we discussed in our column on April 20.







But the economy is not the only preoccupation of President Trump at the moment. After putting the popular video-sharing social medium *Tik Tok* under scrutiny for representing a possible threat to national security, Donald Trump said he was ready to ban its operations in the US, where it counts around 50 million users. The company responded that the data it collects is stored in US-based servers (confirming once again how relevant the concept of digital sovereignty is becoming), with limited and controlled access from its employees. Some read Trump's move as a way of either jeopardising the potential sale of the US arm of *Tik Tok* to Microsoft, or as an attempt to reduce *Tik Tok*'s price.

This is yet another confirmation that one of the main battlefields of the ongoing Cold War 2 between US and China is the tech race between the two superpowers. In a separate, but related field, our recent report on the "stunning" alliance between China and Iran discusses how Cold War 2 is taking shape in the more traditional domain of strategic alliances.

While all of this is going on, the Democratic contender in the November race, Joe Biden, will soon announce the choice of his running mate. Many see this as a potential turning point in the campaign. Biden is set to choose a candidate who, unlike himself, is not old, or male, or white, and for this reason the most credited contenders for the position are Susan Rice and Kamala Harris. But this choice must be considered in the broader context of the US presidency.

Biden, if elected would at 77 years old be the oldest US president in history at the time of his inauguration. He already hinted at the possibility of running for only one term, making his VP the natural candidate for succession in 2024. There is also a possibility that Biden could resign during his first term, which would of course directly make his VP ascend to the presidency. Knowing all this, any Republican voters or swing voters who might be inclined to vote for Biden just to make sure that Trump is not re-elected in November, might want to be reassured that Biden's running mate is as mainstream a politician as possible.

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Looking Ahead

The Week Ahead: US Labor Market To Weaken, EZ Retail Sales To Stabilize; CBs To Maintain An Easing Bias

In the US, nonfarm payrolls are expected to decline (c: 2.26m; p: 4.80m), as the job market's recovery loses pace.

In the EZ, for the first time since March 'annual retail sales' are set to turn positive (c: 0.2% y-o-y; p: -5.1).

In the UK and Australia, the BoE and RBA are expected to keep unchanged their policy stance.

The Quarter Ahead: Global Recovery Hampered By Covid-19 Resurgence; Fed To Strengthen Forward Guidance

The virus: i) continues to spread rapidly in the US, Brazil, India, Russia, and South Africa; and ii) has re-emerged in some areas of Europe, Japan, and China. At the current pace of about 290k infections a day, by the end of 2020 there could be more than 50m infections worldwide. New outbreaks will likely prompt political leaders to re-impose full or partial lockdowns, hindering prospects for an economic rebound in H2-2020.

In the latest move to curb China's power in global technology, President Trump stated he could ban the popular Chinese-owned app TikTok over data collection concerns.

In the US, Fed Chair Powell stated that the CB's 'review of strategy, tools, and communications' will soon be finalized, and will likely introduce stronger forward guidance – by "linking policy adjustments to specific thresholds for inflation and/or unemployment".

Last Week's Review

Real Economy: COVID-19 Spreads Widely. Global Recovery At Risk, Central Banks To Keep Easing Stance

In the US, Q2 GDP contracted at an annualized -32.9% q-o-q (c: -34.1; p: 5.0). A fall in consumer spending accounted for most of the decline – in particular, 'spending on services' plunged -42.5% y-o-y. For a second consecutive week, the number of workers applying for 'initial unemployment benefits' rose (a: 1.43m; c: 1.45m; p: 1.42m), highlighting the fragility of the rebound. Business spending increased slightly: non-defense capital goods excluding aircraft rose 3.3% m-o-m (c: 2.3; p: 1.6). In June: i) PCE rose 0.8% y-o-y (p: 0.5); while ii) core-PCE softened 0.9% y-o-y (c: 1.0; p: 1.0). The Fed: i) left its policy rate near zero; ii) reiterated its pledge to increase its USTs and MBSs holding 'at least at the current pace'; iii) extended its emergency programs through to the end of 2020; and iv) extended its USD-liquidity swap lines through to March 2021.

In the EZ, Q2 GDP shrank at an annualized -40.3% q-o-q – equivalent to a non-annualized -12.1% q-o-q (c: -12.0; p: -3.6); with: i) Spain (a: -18.5% q-o-q; c: -16.6; p: -5.2); and ii) France (a: -13.8% q-o-q; c: -15.3; p: -5.9) amongst the hardest-hit economies. So far, job-furlough programs have prevented a sharp rise in unemployment readings (Jun., a: 7.8%; c: 7.7; p: 7.7). In July: i) CPI inflation rose above expectations at 0.4% y-o-y (c: 0.2; p: 0.3); and ii) core-CPI rose 1.2% y-o-y (c: 0.8; p: 0.8). While inflation remains well below the ECB's 2% target, several EZ economies reported deflation, including Spain (a: -0.6% y-o-y; p: -0.3).

In Japan, June retail sales fell for the fourth consecutive month, as consumer sentiment remains impaired; however, the pace of decline was far slower than expected (a: -1.2% y-o-y; c: -6.5; p: -12.5).

Financial Markets: Liquidity-Driven Performance: Equities And Havens Strengthened; Oil Flat

Market drivers: Three drivers: i) a deteriorating global outlook; ii) negative US real rates; and iii) currency debasement fears, supported the simultaneous rise of bonds, equities and gold – as the USD weakened.

Equities: w-o-w, global stocks rose (MSCI ACWI, 0.7%, to 552) led by the US (S&P 500, +1.7%, to 3,271), where technology buoyed the S&P500 and offset disappointing industrial earnings. EZ stocks declined (Eurostoxx 50, -4.6% to 3,174).

Fixed income: w-o-w, global debt indices rose (BAML Global, +0.3% to 298.9). Across DMs yields fell (10y UST, -5bps to 0.54%; 10y German bund, -9bps to -0.53%).

FX: w-o-w, the USD spot index continued to weaken (DXY, -1.1% to 93.349), closing the worst month in a decade. As a result, DM (EUR/USD, +1.0% to 1.177; GBP/USD, +2.3% to 1.309) and EM currencies (MSCI EMs FX, +0.3% to 1,612) strengthened. In the short-term the USD is weighed down by: i) potential economic weakness – if compared to other DMs – as the pandemic spreads; ii) polarized domestic politics – especially when compared to Europe where the recent EU recovery fund has strengthened the region's unity; and iii) expectations of additional fiscal and monetary stimuli. Over the next few years, the USD will hold its reserve position – as there are no sufficiently deep and liquid reserve-currency alternatives.

Commodities: Oil prices stagnated (Brent, -0.1% to 43.3 USD/b). Gold soared (Gold, +3.9% to 1,975 USD/Oz.), as investors seek a 'store of value' and a safe-haven alternative to the USD.



@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



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