



R&R Weekly Column
By Brunello Rosa



Biden's Budget Highlights His Ambition To Revive The US Economy

US President Joe Biden gave [a speech in Cleveland last week](#), in which he provided his vision for the future of the US economy. He highlighted the importance of putting the middle class back at the centre of his project to rebuild the economy after the pandemic, partly at the expense of the wealthiest 1% of US citizens and large US corporations. Following the speech, he revealed his first, ambitious, USD 6tn annual budget, which Congress needs to pass by the end of September. The budget is large (as was the last budget of the Trump administration, at USD 4.8tn), and it comes in addition to both the USD 1.9tn Covid stimulus bill approved earlier this year and the USD 2.2tn infrastructure plan (which has now been reduced to USD 1.7tn).


This potentially transformative bill [will allocate](#) more than USD 800bn to fight climate change, including investments in environmentally-friendly energy, USD 200bn to provide free pre-school places for all 3-year-old and 4-year-old kids, USD 109bn for two years of free community college for all US students, USD 225bn for a national paid family and medical leave programme, USD 115bn for road and bridge repairs and USD 160bn for public transit and railways, and USD 100bn to improve access to broadband internet for every US household. It also includes USD 1.5tn for operating expenditures for the Pentagon and other government departments. To pay for this increased expenditure, the US administration proposes to increase the taxes on corporations from 21% to 28%, increase capital gains and the top income tax bracket to the tune of USD 3tn, and run a fiscal deficit of over USD 1.3tn over the next decade. The combined effects are expected to push the US debt-to-GDP ratio to 117%, a level not seen since WWII.

This budget will reinforce the fears, discussed in our previous columns (on [May 3](#) and [May 17](#)) that the US economy will overheat over the next few years, thus leading to a rise in inflation, which eventually the Federal Reserve will have to stave off with a rise in interest rates, thus potentially leading to a recession. In effect, inflation has been rising in the last few months, with even the closely watched (by the Fed) headline personal consumption expenditures (PCE) gauge reaching 3.6% y/y in April, with core PCE having reached 3.1% y/y in April (a level not seen since 1992), up from the 1.9% recorded in March. For reference, the standard consumer price index (CPI) was up by 4.2% in April. [We expect inflation prints to remain high](#) in the next few months.

In spite of some investor worries, the Federal Reserve remains relatively relaxed about these increases in inflation, which are still considered to be transient. Even recently, Fed Vice Chair [Richard Clarida reassured](#) the market that the Fed will look through temporary spikes in inflation due to base and supply-bottleneck effects. Even if [the minutes of the April FOMC meeting](#) showed that several FOMC participants were willing to begin a discussion on tapering asset purchases in the next few months, the probability of a rate increase in the near term is very low. We do not expect a rate increase to occur before 2023 at the very earliest.

The market is jittery, but ultimately seems willing to follow the lead of the central bank. The USD remains weak versus the EUR, CAD, AUD, and NZD, among others. The 2y Treasury yield, at 0.14%, is still very close to the middle of the 0-0.25% range for the Fed funds target, and the 10y Treasury yield still remains at 1.58%, a level that is indicative of the fact that inflation expectations are not running out of control.

Our Recent Publications

 [Market Review And Outlook: Vaccine Rollouts And Abundant Liquidity To Support Market Performance](#), by Alessandro Magnoli Bocchi and Fawaz Sulaiman Al Mughrabi, 21 May 2021

 **GEOPOLITICAL CORNER:** [Looking Beyond its Covid Tragedy, India Remains the World's Most Significant Rising Power](#), by John C. Hulsman, 18 May 2021



Looking Ahead

The Week Ahead: US Unemployment To Fall While EZ Inflation Rate Is Expected To Rise

In the US, in May, non-farm payrolls are expected to increase to 650k (p: 266k), while the unemployment rate is expected to fall slightly to 5.9% (p: 6.0%).

In the EZ, April's retail sales are expected to climb to 26% y-o-y (p: 12.0%), and the inflation rate is expected to rise to 1.9% y-o-y (p: 1.6%), with core-inflation rising to 0.9% y-o-y (p: 0.7%).

The Quarter Ahead: Global Vaccine Distribution To Face Delays; US Budget Increase; CBs To Maintain Their Easing Bias

The surge of the COVID-19 in India and lower-than-expected vaccine supplies in Q2-2021 are likely to have a negative impact on global recovery prospects. Concretely, by the end of June COVAX will face a shortfall of 190m doses; however, its original objective – delivery of 2bn doses of vaccines worldwide in 2021, and 1.8bn doses to 92 lower income economies by early 2022 – are still well within reach.

Amid rising COVID-19 cases globally, US president Joe Biden ordered his intelligence agencies to “review the evidence for the lab-leak hypothesis”, and to report the findings back to him within 90 days. China continues to deny the possibility of lab leak.

US Senate Republicans have blocked the creation of a bipartisan panel to study the January 6 attack on the Capitol, in a show of party loyalty to former president Donald Trump. The vote was 54 to 35 – short of the 60 votes needed to take up a House-passed bill.

The Biden administration released its budget for fiscal year 2022, calling for increases in spending on: i) education; ii) healthcare; and iii) renewable energy. President Biden proposed a USD 6tn budget for the year beginning October 1, including USD 1.5tn in discretionary spending for the military and domestic programs.

In the US, the Fed seems willing to start reducing the pace of asset purchases; yet, any real action is likely months away. Fed officials have reiterated that price pressures including: i) fiscal stimulus; ii) supply constraints; and iii) rising commodity prices are transitory.

Last Week's Review

Real Economy: DM Economic Recovery Still Fragile As Vaccine Delays Hinder Growth Outlook

In the US, April's orders for ‘non-defense capital goods excluding aircraft’ – a closely watched proxy for business spending plans – jumped by 2.3% (c: 0.8%; p: 1.6%). April's ‘durable goods orders’ fell to -1.3% (c: 0.7%; p: 1.3%), showing the first decline in almost a year, as supply shortages continued to impact production.

Still in the US, in April: i) the PCE price index rose faster-than-expected to 3.6% y-o-y (c: 2.2%; p: 2.4%), as price pressures built in the rapidly expanding US economy; and ii) core-PCE price index – the Fed preferred inflation gauge – rose to 3.1% y-o-y (c: 2.9%; p: 1.9%), marking the highest rate since the 1990s, and bringing it well above the Fed's 2% average target.

In the EZ, May's consumer confidence indicator rose in line with consensus to -5.1 (c: -5.1; p: -8.1), up for the fourth month in a row to the highest level since October 2018, supported by: i) the gradual reopening of the economy; and ii) an acceleration in the COVID vaccination pace.

In New Zealand, during its May meeting, the RBNZ held its Official Cash Rate (OCR) unchanged at 0.25%, but projected a 25bps rate hike to 0.50% by September 2022 - reaching 1.50% by the end of 2023.

Financial Markets: Global Equities And Bonds Rise; USD Flat; Oil Prices Near 70 USD/B

Market drivers: optimism about the reopening of the US economy and prospects of robust economic recovery fueled by: i) massive government spending; and ii) ultra-loose monetary policy supported risk-on sentiment.

Global equities rose w-o-w (MSCI ACWI, +1.4%, to 711). In the US, growth shares outperformed their value counterparts; Facebook and Google parent Alphabet helped communication services stocks outperform within the S&P 500, and a rebound in Tesla boosted consumer discretionary shares (+1.2%, to 4,204). In the EZ, European stocks advanced on continued affirmations of ultra-easy monetary policy and reports of a massive US fiscal spending plan (Eurostoxx 50, +1.1%, to 4,071).

Fixed Income: w-o-w global bonds rose (BAML Global, +0.3% to 292.7) and UST yields fell (-4bps, to 1.59%), as a reading on inflation came in higher than expected.

FX: w-o-w, the USD was flat (DXY, 0%, to 90.031; EUR/USD +0.1%, to 1.219).

Commodities: Oil prices rose (Brent, 4.8% to 69.6 USD/b), as signs of a brighter global demand outlook more than offset concerns over potentially more Iranian supply. Gold prices climbed (+1.2% to 1,903 USD/Oz) as UST yields retreated and the USD eased off of its more than two-week highs.



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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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