



**R&R Weekly Column**  
**By Brunello Rosa**



## The “Triangle of Death” of EU Elections is About To Begin

A couple of years ago, when the pandemic was not even on the horizon and populist parties were on the rise throughout Europe, [we identified](#) the September 2021 – June 2022 period as the moment of truth for European politics. Three key elections at the EU (and Eurozone) level will take place during this period. First, on Sunday 26<sup>th</sup> September, the German general election will take place. Several months later, in February 2022, will be the Italian Presidential election (carried out by a special electoral college, including all MPs and regional representatives). Finally, in April there will be the French Presidential election, which in turn will be followed by France’s parliamentary elections in June. As we discussed in depth [in a previous analysis](#), if any of those crucial events were to result in the victory of anti-system, anti-European candidates, the European integration process may stall indefinitely, and perhaps reverse further than it has already with Brexit.


As we discuss further in our forthcoming preview of the German election (after the in-depth [analysis we published recently](#)), the race has become more interesting than one could have expected. The choice of unsuitable candidates from the Greens (Annalena Baerbock) and the CDU/CSU (Armin Laschet) for the Chancellorship has given an unexpected boost to the SPD candidate Olaf Scholtz, who is [now clearly leading the polls](#). Many combinations and permutations of coalitions will be attempted after the vote, but if the actual votes confirm the polls then it seems that a three-party coalition will be needed to form a government in Germany, for the first time since WWII. The so-called “traffic-light” SPD-Liberals-Greens coalition and the so-called “Jamaica” CDU-Liberal-Greens coalition appear to be the most likely to emerge. These coalitions are likely to be tenuous at best, and prone to collapse given cultural and political differences. The point is this: if Germany becomes politically unstable, that cannot be good either for Germany or – most importantly – for the EU and its integration process.

The Italian presidential election is also going to be a crucial moment. All eyes will be on Mario Draghi, and whether he will move from [Palazzo Chigi to the Quirinale Palace](#). This could mark the beginning of renewed political instability in Italy, or the interruption of the reform project undertaken by Draghi’s government as a result of the Next Generation EU plan. The importance of the President in Italy is often underestimated, as is the crucial role Italian presidents have played in dampening the populist pushes within the country’s political system, or in preventing severe deviations from the Constitutional norm and spirit from taking place. Italy remains a cornerstone of the European project (one of the six founding members), and we have already seen how problematic EU policymaking becomes when Italy elects anti-system or populist leaders.


The French Presidential election is also crucial, especially if Germany become less of a bastion of stability in Europe. In theory, President Macron should have a relatively easy ride towards being re-elected, but in reality [Marine Le Pen continues to be very close to President Macron in the polls](#) for the second round of another election between them. Needless to say, if Le Pen were to become President, this would be yet another “French revolution”, which would likely mark the end of the EU integration process. President Macron still has time to recover, but he is going to face an uphill battle in this campaign.


In conclusion, the EU is about to enter its most delicate period of any time in the last few years, with the EU integration process at risk of derailment in coming months. A political derailment of this kind would have clear implications for the ECB’s policy stance and market dynamics.

### **Our Recent Publications**

 [Flash Preview: Bank Of Japan To Delay Scaling Back Its Covid-Related Emergency Measures](#), by Brunello Rosa and Fawaz Sulaiman Al Mughrabi, 16 September 2021

 [Flash Preview: Bank Of England To Stay On Hold While Inflation Soars](#), by Brunello Rosa and Karmen Meneses, 16 September 2021

 [Flash Review: The ECB Recalibrates PEPP by Moderately Reducing The Pace of Purchases](#), by Brunello Rosa, 9 September 2021

 **GEOPOLITICAL CORNER:** [A Necessary Fork In The Road: The End Of Nation-Building In Afghanistan And The West’s Great Power Future](#), by John C. Hulsman, 7 September 2021



Looking Ahead

The Week Ahead: PMIs Expected To Decline In Developed Markets

**In DMs**, manufacturing PMIs are expected to soften, as: *i)* US activity remains stable (c: 61.1; p: 61.1); *ii)* EZ activity slows (c: 60.5; p: 61.4); and *iii)* Japan's indicators shows weaker activity (c: 51.5; p: 52.7). DM services PMIs are also likely to slow down (US: c: 54.9; p: 55.1; EZ: c: 58.7; p: 59.0; Japan: c: 43.0; p: 42.9).

The Quarter Ahead: Lingering Downside Risks Continue To Weigh On Economic Outlook; Central Banks Turn Hawkish

**Geopolitical tensions to rise. US announces a new security alliance with UK and Australia, to counter China.** US President Biden announced a new working group with UK and Australia "to share advanced technologies", including the acquisition of nuclear-powered submarines - in a bid to counter China. The trio, now known by the acronym 'AUKUS', will share information in key technological areas such as: *i)* AI; *ii)* cyber; *iii)* quantum; *iv)* underwater systems; and *v)* long-range strike capabilities.

**France recalls its ambassadors to the US and Australia.** The French government recalled its ambassadors in "protest of the trilateral security deal that included nuclear-powered submarines for Australia".

**China enters Taiwan air defense zone.** A day after Taiwan announced a USD 9bn boost to military spending "to counter the threat from China", the island's air force scrambled to warn away 10 Chinese aircraft that entered its air defense zone. Chinese-claimed Taiwan has complained of repeated missions by China's air force near the democratically governed island, often in the southwestern part of its air defense zone - close to the Taiwan-controlled islands.

**World Bank changed data to boost China ranking.** The World Bank is cancelling a prominent report on business conditions around the world after investigators found staff members were pressured by the bank's leaders to alter data about China, and some other governments. The bank said it would discontinue "Doing Business" following an investigation prompted by internal reports of "data irregularities" in its 2018, and 2020 editions and possible "ethical matters" involving bank staff.

**Central Banks to determine "the right time" to begin normalizing monetary policy.** A few CBs are ready to hike rates, some are in the process of tapering, and some have maintained their easing stance. At this week's FOMC meeting, the markets will look for more hints of Fed tapering by the end of 2021, but it is unlikely to obtain: 1) specific dates; or 2) pace of the reduction.

Last Week's Review

Real Economy: Economic Growth Hindered By Lingering Risks, Inflation Pressures Transitory

**In the US**, August's retail sales rose by 0.7% m-o-m (c: -0.8%; p: -1.8%). September's consumer sentiment index fell to 71.0 (c: 72.2; p: 70.3), as consumers - worried by the spread of the COVID-19 delta variant - expect "the least favorable prospects in more than a decade".

**In the EZ**, July's IP rose more-than-expected to 7.7%y-o-y (c: 6.0%; p: 10.1%).

**In the Japan**, July's machinery orders fell to 11.1% y-o-y (c: 15.7%; p: 18.6%).

**In the US**, August's inflation rate came in at 5.3% y-o-y (c: 5.3%; p: 5.4%), and 'core inflation' at 4.0% y-o-y (c: 4.2%; p: 4.3%).

Financial Markets: Global Stocks Weaken; Bond Remain Flat; A Stronger USD Weighs On Gold

**Market drivers:** investors remain cautious ahead of: *i)* a highly-anticipated FOMC meeting, in which the Fed is expected to provide more details on its tapering timeline; *ii)* upcoming economic data painting a mixed scenario, increasing their doubts on when the Fed will start cutting stimulus; and *iii)* a disappointing US consumer sentiment.

**Global equities** fell w-o-w (MSCI ACWI, -1.0%, to 730). In the *US*, the S&P 500 Index retreated to a one-month low (-0.6% w-o-w to 4,433), dragged down by materials and technology sectors. In the *EZ*, shares weakened (Eurostoxx 50, -0.9% to 4,131), as: *i)* concerns about the impact of the COVID-19 delta variant on the global economy outweighed expectations of continuing CB support. In *EMs*, equities fell (MSCI EMs, -2.3%, to 1,279), as Chinese stocks kept dropping (Shanghai Comp., -2.4%, to 3,614), dragged down by Beijing's regulatory crackdown after a series of overhaul on industries, and resurging - although sporadic - COVID-19 cases. *Volatility* fell slightly (VIX S&P 500, -0.2 points to 20.8, 52w avg.: 21.3; 10y avg.: 17.3).

**Fixed Income:** w-o-w global bonds remained stable (BAML Global, -0.2% to 296.6) and UST yields rose slightly (+2 bps, to 1.36%), as investors await further details on when the Fed will start cutting stimulus.

**FX:** w-o-w, the US Dollar Index rose slightly (DXY, +0.7%, to 93.195; EUR/USD -0.8%, to 1.173), the second weekly gain. In *EMs*, currencies fell against the USD (MSCI EM Currency Index, -0.4% to 1,732).

**Commodities:** Oil prices rose (Brent, +3.3% to 75.3 USD/b), due to: *i)* supply disruptions; and *ii)* data from both the EIA and API showing a decline in crude stocks. Gold prices weakened (-1.9% to 1,754 USD/Oz), amid a USD surge ahead of the FOMC meeting this week.



@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](mailto:info@rosa-roubini-associates.com)

[www.rosa-roubini-associates.com](http://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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