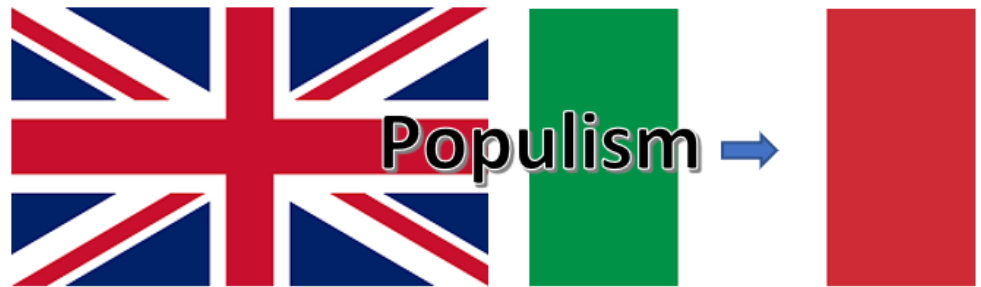




*R&R Weekly Column*  
*By Brunello Rosa*



### Populism Is On The Way Out In The UK, But On The Way Back In Italy

The last few weeks have been extremely intense from a political risk perspective. First (as we discussed in [a recent column](#)), the UK government nearly collapsed after a rebellion – almost a mutiny – of a large part of its components took place, which effectively forced Boris Johnson to resign from his position as leader of the Conservative Party. Johnson said he will remain as PM until a successor is found, which will happen on September 5<sup>th</sup>. Then [in Italy a sudden government crisis](#) initiated by M5S leader Giuseppe Conte led to the dissolution of parliament and early elections, which will take place on September 25<sup>th</sup>. PM Draghi will remain in power until then, to discharge the government's "current affairs."

Incidentally, one may notice how Boris Johnson and Mario Draghi have been among the fiercest opponents to Putin in his war in Ukraine. The [UK was certainly the largest provider of weapons to Kyiv](#). [Italy has been the most decisive proponent of a European "price cap" on gas](#), a measure that requires the support of the US for an effective enforcement, which would damage Russia's energy revenues far more than the embargo on oil imports, as the latter merely reduces the quantity of oil available and so increases the prices. These two fierce enemies of Vladimir Putin will be soon out of power.

The question is: who is going to come to power after these two leaders?

In the UK, it seems that the populist era is about to finish with the end of Johnson's tenure in office. The race for succession in the Tory party is now down to two main candidates: Rishi Sunak and Liz Truss. [The differences in policies between the two are not massive, but are still significant](#). Each candidate represents a different era of the Conservative party. Sunak supports a return of the "old" tradition of the Tory party of being fiscally prudent; it has led to the proposed increases in national insurance contributions to finance the expansion of the NHS after the pandemic, as well to as an increase in corporate tax rates. Liz Truss meanwhile speaks to the more neo-liberalist component of the party, which seeks lower taxes to boost growth.

In both cases however, it seems that the period of "comforting fairy tales" – to use Sunak's expression in his letter of resignation from Chancellor – for example, of the positive impact of Brexit on the UK economy, is over with the end of Johnson's populist premiership, and a return of a more pragmatic and less ideological Tory leadership is imminent.

In Italy the opposite seems to be happening. After 17 months of the technocratic government led by Mario Draghi, which allowed Italy to start reaping the benefits of the EU's Recovery plan, all signals point to a possible victory of the centre-right coalition. Each component within such a coalition is a reason for concern, to say the least.

The old patriarch of the coalition, Silvio Berlusconi, is the man who brought back populism in Italy after the fall of the so-called first republic. His first promises now (to increase to EUR 1,000 per month each pension below that threshold) are already reminiscent of the famous "less taxes for all" of 1994, when he won his first election. Just to give an idea of what his return to power could mean, fulfilling that promise alone would cost at least EUR 60bn, three times what Italy will get from the EU if it respects all the milestones of the Recovery plan by December.

Matteo Salvini's Lega meanwhile continues to have anti-Euro positions even after participating in Draghi's government. Those positions already led to a large widening of bond spreads in 2018, at the time of the M5S-Lega government. Finally, Giorgia Meloni's Brothers of Italy, which enjoys the leading position in voting intentions (around 23-24%) according to recent polling, is an almost unknown quantity. As the [New York Times recently said](#) (in an article titled "The Future Is Italy, and It's Bleak"), what most people know about Meloni and her party is that they come from the post-fascist tradition, and that its economic plans are obscure.

Clearly there is a risk of a return to populism with a vengeance after the September election in Italy. Such a return would likely lead to a renewed widening of intra-EMU spread, [which the ECB will have hard time to consider "unwarranted,"](#) as it did already in 2018.

#### Our Recent Publications

Flash Review: The ECB Hikes More Than Expected  
Thanks To Its New Transmission Protection Instrument,  
by Brunello Rosa and Nato Balavadze, 21 July 2022



Flash Preview: ECB To Start Its Policy Rate Normalisation and  
Launch Its Anti-Fragmentation Facility in July, by Brunello Rosa,  
Nouriel Roubini and Nato Balavadze, 15 July 2022

Looking Ahead

**The Week Ahead: Fed To Hike Rates; EZ Inflation To Accelerate; QoQ GDP To Rise Slightly In US And EZ Largest Economies**

**In the US**, in Q2, according to advance estimates, GDP is expected to increase by 0.4% q-o-q (*p*: -1.6%). Core PCE is likely so stay unchanged at 4.7% y-o-y. July's Michigan Consumer Sentiment is seen rising to 51.1 (*p*: 50).

**Also in the US**, the Fed is expected to increase its target Fed funds range by 75 bps to 2.25% - 2.5%.

**In the EZ**, in Q2, according to flash estimates, the economy is seen slowing down to 0.1% q-o-q from 0.6% q-o-q. In July, headline and core inflation is expected to rise to 8.7% y-o-y (*p*: 8.6%) and 3.8% y-o-y (*p*: 3.7%). July's economic sentiment is expected to decrease to 102 (*p*: 104) and consumer confidence is likely to deteriorate further to -27 (*p*: -23.8).

**Among the largest EZ economies**, according to preliminary estimates in Q2, i) France's GDP is expected to advance slightly by 0.2% q-o-q (*p*: -0.2%); ii) German economy is likely to decelerate to 0.1% q-o-q (*p*: 0.2%) and 1.7% y-o-y (*p*: 3.8%); and iii) In Italy, GDP is seen rising 0.3% q-o-q (*p*: 0.1%), whereas it is expected to slow down to 3.7% (*p*: 6.2%).

**The Quarter Ahead: Russia-Ukraine Grain Deal; Russia Restarts Nord Stream 1 Pipeline; The EU Urges Gas Rationing**

**Russia and Ukraine signed an UN-backed deal in Istanbul which allows Kyiv to export grain through the Black Sea.** Amid rising food prices, according to the deal, around \$10 bn worth of grain will be available for sale. The deal expects to resume shipments to pre-war levels of 5 ml tonnes a month. As the UN officials report, Russian and Ukrainian forces will not target any of the commercial vessels or ports involved in the initiative.

**Gas supplies are resumed through Nord Stream 1.** Following a 10-day maintenance break, Russian oil company Gazprom restarted natural gas supplies to Germany. The pipeline is only delivering 40% of its capacity and thus Europe's and especially Germany's energy situation remains uncertain.

**The European Commission asked its member states to reduce their gas use by 15% from August to March.** This voluntary measure is a part of the Save Gas for a Safe Winter Plan presented in Brussels over the fears of a potential cutoff. In the case of severe gas shortage, the Commission might need to make the target mandatory.

Last Week's Review

**Real Economy: Headline Inflation Accelerated, While Core Inflation Fell In EZ And UK; PMIs declined in DMs; ECB Raised Rates**

**In the EZ**, in June headline inflation rose to 8.6% y-o-y (*p*: 8.1%; *c*: 8.6%), whereas core-inflation slightly cooled off to 3.7% y-o-y (*p*: 3.8%; *c*: 3.7%). Monthly inflation stood unchanged at 0.8% as expected. Consumer confidence deteriorated to -27 (*p*: -23.8; *c*: -24.9).

**Also in the EZ**, ECB raise its *policy rates* by 50 bps and launched its *Transmission Protection Instrument* (PTI).

**In the UK**, June's unemployment rate was unchanged at 3.8% (*c*: 3.9%). In June headline inflation surged to 9.4% y-o-y (*p*: 9.1%; *c*: 9.3%), while core inflation eased off to 5.8% y-o-y (*p*: 5.9%) as expected. Monthly inflation rose to 0.8% (*p*: 0.7%; *c*: 0.7%). June's retail sales shrank by -5.9% y-o-y (*p*: -4.7%; *c*: -5.3%).

**In DMs**, business activity declined. i) EZ's manufacturing and services activity fell to 49.6 (*p*: 52.1; *c*: 51) and 50.6 (*p*: 53; *c*: 52) respectively. Composite PMI declined to 49.9 (*p*: 52; *c*: 51); ii) UK's manufacturing and services PMIs slowed down to 52.2 (*p*: 52.8; *c*: 52) and 53.3 (*p*: 54.3; *c*: 53) and composite PMI fell to 52.8 (*p*: 53.7; *c*: 52.5); and iii) In the US, manufacturing and services indicators decreased to 52.3 (*p*: 52.7; *c*: 52) and 53.3 (*p*: 54.3; *c*: 53). Composite PMI fell accordingly to 47.5 (*p*: 52.3).

**Financial Markets: US And EZ Stocks Rose; Yields Fell; Dollar Was Down, While Oil And Gold Prices Rose**

**Market Drivers:** Despite weak economic data and a 50bps rate hike by the ECB, share prices in the US and EZ rose, as investors reacted positively to core inflation slowing down. However, the dampening economic growth weighed on yields, which fell.

**Global Equities:** Increased w-o-w (MSCI ACWI, +3.17, to 617.71). The US S&P 500 index increased (+2.5% w-o-w, to 3,951.63). In the EZ, share prices were up (Eurostoxx 50, +3.4% w-o-w, to 3,596.5). In EMs, equity prices decreased (MSCI EMs, -3.0%, to 990.37). Volatility rose to 25.6 (VIX S&P 500, 52w avg.: 23.0; 10y avg.: 18.1).

**Fixed Income:** w-o-w, 10-year US treasury yields fell (-17.4 bps to 2.75%). The 2-year US Treasury yields decreased too (-15.8 bps to 2.97%). The German 10-year bund yield also fell (-9 bps to 1.04%).

**FX:** w-o-w, the US Dollar Index was down (DXY, -1.3%, to 106.5; EUR/USD +1.2%, to 1.02). In EMs, currencies strengthened (MSCI EM Currency Index, +0.2% w-o-w, to 1,649.29).

**Commodities:** w-o-w, oil prices rose (Brent, +2.6% to 103.6 USD/b). Gold prices also increased w-o-w (+1.3% to 1,725.3 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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