



R&R Weekly Column
By Brunello Rosa



Major Central Banks Will Continue Tightening Monetary Policy

At the end of last week, [the figures for US Non-Farm Payrolls](#) (NFP) were released. The US Bureau of Labour Statistics reported that the US economy added 315K jobs in August of 2022, compared to a downwardly revised 526K in July (p. 528), but above market expectation of 300K and pointing to broad-based hiring across many sectors. Even if [the unemployment rate rose slightly from 3.5% to 3.7%](#), non-farm employment is now 240K higher than its pre-pandemic level in February 2020.

On the basis of these figures, even if employment figures are a lagging indicator of economic activity, it may be correct to say that the US economy is not in a recession, not even a technical one, in spite of two consecutive quarters of contraction. This seems to be confirmed by a cross-check through the lense of the so-called Okun's law, which links unemployment and GDP changes. According to [a recent analysis](#), the US economy may have actually been growing in H1. This is crucial in determining what the Fed, and other major central banks, will do in coming months.

Regarding the Fed, at its traditional gathering in Jackson Hole Chair Powell surprised the market with [unexpectedly hawkish remarks](#). Powell said that the US economy remains strong and the world economy resilient in the face of the ongoing energy crisis deriving from the war in Ukraine, and therefore the FOMC will continue tightening its policy stance. The FOMC will continue aiming for a "soft landing" of the economy, but the Committee priority is now to bring inflation (which is still running at 8.5% y/y) back to target. Commentators and markets read this as an anticipation that another 75bps rate increase will be delivered in September. In July, [Powell clarified that the Fed will not provide as much forward guidance as before](#), as the FOMC has become data dependent, but this seems now a reasonable assumption.

But more than the decisions that the Fed makes in any given meeting, what matters is the cumulative amount of tightening that takes place. In this respect, the Fed has recently reached neutral territory with its policy rate (2.50%), and it is ready to enter restrictive territory with the next rate increase, to reach and overcome the 3-3.25% expected at year-end [according to its SEP dots](#). However, one should note that with inflation at 8.5% and a policy rate at even 3.5%, policy rates would still be negative in real terms, meaning that in real terms the Fed's policy stance remains highly accommodative. To bring inflation down to 2%, much more tightening may be needed.

Regarding the ECB, next week another 50bps rate increase is expected, but perhaps a surprise 75bps hike cannot be ruled out. This follows the [remarks by ECB Board Member Isabel Schnabel](#), who said that the ECB may need to make further "sacrifices" (i.e. rate increases) as the inflation outlook has not improved. Additionally, the ECB's policy stance cannot remain too distant from that of the Fed, at a time when the EUR has already fallen below parity versus the USD. A weaker currency contributes to higher inflation rates, at a time when the ECB is trying to bring inflation back to target.

Our Recent Publications

 [Qatar Prepares for a Historic World Cup](#), by Gulf State Analytics, 2 September 2022



[Restoring The Fed's Credibility Goes Hand In Hand With Fighting Inflation](#), by Filippo Ramigni, 23 August 2022

Looking Ahead

The Week Ahead: EZ QoQ GDP To Advance; PMIs To Fall In DMs; UK Retail Sales To Recover Slightly; CBs To Remain Hawkish

In the US, in August, services and composite PMI are seen falling to 44.8 (p: 47.3) and to 45 (p: 47.7), respectively.

In the EZ, in Q2, according to a third estimate, GDP is expected to rise by 0.6% q-o-q (p: 0.5%) and 3.9% y-o-y (p: 5.4%). In August, services and composite PMI are seen falling to 50.2 (p: 51.2) and to 49.2 (p: 49.9). In July, retail sales are likely to recover slightly to -0.7% y-o-y (p: -3.7%) and 0.4% m-o-m (p: -3.7%).

In the UK, in August, services and composite PMI are seen falling to 52.5 (p: 52.6) and to 50.9 (p: 52.1), respectively.

Also in the EZ, the ECB is expected to increase its key interest rates by 50 basis points. But a 75bps hike is also considered.

The Quarter Ahead: Russia Announced Indefinite Shutdown Of Pipeline; EU Restricted Russian Visas; Japan Back To Nuclear Power

Russia's Gazprom announced an indefinite shutdown of the Nord Stream 1 pipeline. The decision was taken after G7 countries supported price cap on Russian oil to limit Moscow's ability to finance the war in Ukraine. Russian state energy giant cited mechanical problems, detecting an oil leak at its compressor station. In June, Gazprom already cut capacity, which supplies for about 35% of Europe's total Russian gas imports, and the complete shutdown deepens the recession risks in the EU.

EU foreign ministers decided to make it more expensive as well as difficult for Russians to obtain EU visas. The E.U. was divided to agree on a blanket ban. France and Germany oppose visa ban for all Russians. The announcement says that: 'Our visa policies should reflect that and continue to allow for people-to-people contacts in the EU with Russian nationals not linked to the Russian government.'

Biden administration formally approved its intent to sell to Taiwan USD 1.1 bn worth of defensive arms. The package includes anti-ship missiles and air-to-air weapons. As the spokesperson for the Chinese Embassy in Washington reported, the possible arms sales 'severely jeopardizes China-U.S. relations and peace and stability across the Taiwan Strait'.

Japan signals a return to nuclear power amid soaring fuel prices. Tokyo is planning to extend ageing reactors' lifespan and develop new nuclear power plants. Most of Japan's nuclear plants were suspended after the 2011 Fukushima disaster.

Last Week's Review

Real Economy: EZ Inflation Rose; US NFP Softened; French And Italian QoQ GDP Rose; Manufacturing PMI Fell In DMs

In the US, in August, the unemployment rate edged up by 3.7% (c: 3.5%; p: 3.5%) and NFPs decelerated to 315K (c: 300K; p: 526K). Still in August, manufacturing PMI decreased to 51.5 (c: 51.3; p: 52.2).

In the EZ, in August, headline and core inflation rates rose to 9.1% y-o-y (c: 9.0%; p: 8.9%) and 4.3% y-o-y (c: 4.1%; p: 4.0%) respectively. Also in August, economic sentiment decreased to 97.6 (c: 98; p: 98.9), whereas consumer confidence recovered slightly to -24.9 (p: -27) as expected. August's manufacturing PMI fell to 49.6 (c: 49.7; p: 49.8). In July, the unemployment rate decreased to 6.6% (p: 6.7%). July's PPI rose by 37.9% y-o-y (c: 35.8%; p: 36.0%).

In the UK, in August, manufacturing PMI fell to 47.3 (c: 46; p: 52.1)

Among the largest EZ economies, in Q2 French GDP rose by 0.5% q-o-q (p: -0.2%) as expected and Italian GDP advanced by 1.1% q-o-q (c: 1.0%; p: 0.1%).

Financial Markets: Stocks Fell, Whereas Yields Rose; Dollar Is Up; While Oil And Gold Prices Are Down

Market Drivers: Hawkish messages from Fed officials weighed on stocks. 2-year yield recently hit the highest level since 2007, as investors anticipate rate hikes. Moreover, a significant slowdown in private payroll growth pushed yields up.

Global Equities: Decreased w-o-w (MSCI ACWI, -3.1%, to 608.31). The US S&P 500 index decreased (-3.3% w-o-w, to 3,924.26). In the EZ, share prices were down (Eurostoxx 50, -1.6% w-o-w, to 3,544.38). In EMs, equity prices decreased (MSCI EMs, -3.0%, to 976.1). Volatility rose to 26.65 (VIX S&P 500, 52w avg.: 24.3; 10y avg.: 18.2).

Fixed Income: w-o-w, 10-year US treasury yields rose (+16.5 bps to 3.20%). The 2-year US Treasury yields rose as well (+1.3 bps to 3.40%). The German 10-year bund yield rose (+10.9 bps to 1.51%).

FX: w-o-w, the US Dollar Index was up (DXY, +0.8%, to 109.58; EUR/USD 0.0%, to 0.99). In EMs, currencies fell (MSCI EM Currency Index, -0.7% w-o-w, to 1,636.25).

Commodities: w-o-w, oil prices fell (Brent, -5.8% to 93.28 USD/b). Gold prices decreased w-o-w (-1.6% to 1,722.6 USD/Oz).



@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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