

All eyes on Europe

Europe might be losing international competitiveness, but in the coming days it will return to the global centre stage with three major events: the ECB's rate cut decisions, European elections and, of course, the European Football Championship



Christine kicks it all off

Europe is back in the global spotlight, if only for the summer. Off the pitch, the most remarkable action is clearly the ECB's rate cut decision. The European Central Bank rarely starts an easing or tightening cycle before the US Fed. And the latest cut is even more remarkable as it comes despite accelerating inflation and wage growth amid a cyclical rebound in the eurozone economy.

If it hadn't banged on about it so much over the last couple of months, the June rate cut would hardly have been needed. In the past, rate cut cycles were always triggered by either a recession or a severe crisis; fortunately, we don't have either right now, so this is another unprecedented event. After a pandemic, lockdowns, war and an energy crisis, maybe such unprecedented action is realistically 'normal' and hopefully won't turn out to be a policy mistake within a couple of months.

And the rate cut decision demonstrates a shift within the ECB itself. It's regained confidence in its own forecasting skills and takes enough comfort from the benign inflation forecast from the

second half of 2025 onwards to justify cutting rates. It's like Asterix and his magic potion. All of a sudden, the forecasts debunked and questioned by the ECB itself over the past few years have become powerful and influential again. There's nothing wrong with that, and the rate cut decision also marks an attempt to become a real forward-looking central bank again. Better perhaps than an uncertain institution preoccupied with backwards-looking data. It's certainly an interesting experiment, and it won't just be markets but other central banks who'll be watching closely.

Electoral dysfunction

The European elections have already started and will continue to resonate well beyond the result declarations. Anti-European parties will, no doubt, grab the initial headlines. Far more interesting in the longer term, however, will be the makeup of the European Parliament and its institutions and whether it and the European Commission will be able to foster more growth-orientated initiatives and plough on with further integration. The elections will also have repercussions for national politics should national governing parties lose too much support. I'm thinking notably of France and Germany here.

That said, don't expect any immediate economic impact from the elections. As is so often the case with Europe, any change is gradual and becomes more visible through the rear-view mirror rather than the windscreen.

Lagarde up front

And, if that weren't exciting enough, we have Euro2024, the European Football Championship. It kicks off in Germany, where there's some hope that something like 'soccer-nomics' does actually exist, lifting the economy out of stagnation and magically making the need for investments and structural changes disappear. Fat chance, I'm afraid. As much as I sympathise with the notion, the economic research released in the run-up to international sporting events is always more optimistic than the reality afterwards.

But hey, even if there's no long-lasting economic impact, let's enjoy some interesting decisions, results and matches... with Christine Lagarde playing up front.

Our key calls this month

- **United States:** The US economy has proven to be remarkably resilient to high interest rates, but there are some signs of stress. By September, we expect to see at least two more cooler inflation readings, and that should be enough to unlock a rate cut – particularly if we also see further slack emerge in the jobs market. We expect three rate cuts this year.
- **Eurozone:** The economy continues to recover, but there are no reasons to expect a significant acceleration in growth. With some pockets of inflationary pressures still hanging around, the ECB's rate cutting cycle will unfold very slowly. We expect at most two further cuts this year.
- **United Kingdom:** We're still expecting an August rate cut from the Bank of England, despite some stubborn services inflation data and the surprise announcement of an early election.
- **China:** Key economic indicators are mixed in China but were mostly weaker than expected last month. July's Third Plenum meeting will likely provide further details on the longer-term

policy direction, which may include measures on supporting property, employment, and childcare.

- **Central and Eastern Europe:** The CEE region's economic recovery continues and we expect this to continue in the months ahead, although the data is mixed. Inflation has also picked up and is expected to head more to the upside in most of the region, complicating further monetary easing.
- **FX:** Some softer US data has managed to pull the dollar away from its highs of the year. Our baseline Fed scenario should see the dollar drift lower over coming quarters, although the US elections remain the wild card.
- **Market rates:** Usually, rate cuts are good for bonds. However the outlook is clouded by a lack of clarity on the extent of ECB cuts ahead – and a Fed that remains constrained by inflation data. We see further upside to US long-term rates over the coming weeks.

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