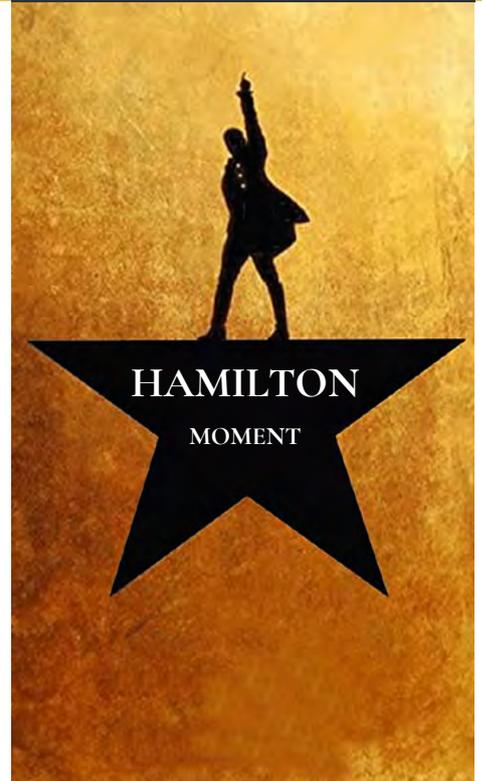




Imagine

LATEST



Normally, most of this weekly update is spent discussing the US and China and for good reason since those two economies are the ones driving all other economies forward.

It is almost as if Europe and Japan are passengers on the train as opposed to being part of the engine. However, imagine a future where the Eurozone gets its act together.

Potential power of the Eurozone

The Eurozone has 340m people, roughly the same as the US. If the Eurozone was to get its act together then this would be a powerful thing for the world. This week, investors glimpsed what a united Eurozone might look like. Since the global financial crisis in 2007, the Eurozone has been dogged by the imbalances created by its own incomplete architecture. Whilst the Eurozone has a central bank – the European Central Bank (ECB) – fiscal policy is left to member countries. It is as though the foundations of the house have been built along with the walls but there is no roof. It is too early to declare this with certainty but what if the Eurozone just got a roof?

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In late May came the announcement that French President Macron and German Chancellor Merkel potentially conjured up a 'Hamilton' moment. You may have seen the musical Hamilton, based on the story of Alexander Hamilton who in 1790 paved the path to the creation of the US's federal system. In essence, his idea was to transfer the Revolutionary War debts accrued by the states to the federal government and then let President Washington levy taxes and issue treasury securities to repay those obligations.

According to Bloomberg, French and German governments have made a proposal for €750bn in bonds to finance European wide coronavirus relief that would be raised in common, not by any constituent state. So, this might be Europe's Hamilton moment.

This plan still faces many hurdles since a group of four EU countries are already lobbying against it, but this development is a positive sign that France and Germany were able to come to an agreement proactively without markets having to force their hand. There is a sense among investors that this might be a real turning point for the Eurozone if the proposal becomes law.

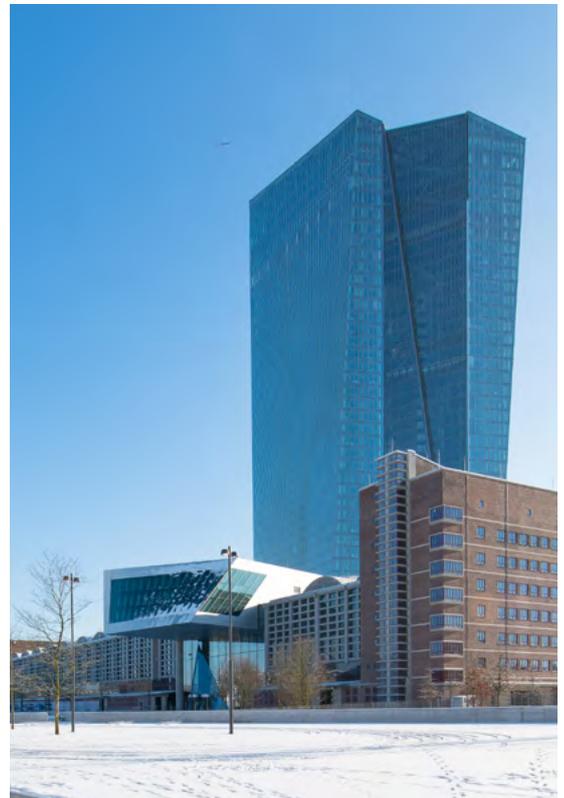
Germany announce post-coronavirus stimulus plan

However, this is not the extent of the good developments. This week, overturning years of fiscal orthodoxy, Germany has become the first big European country to announce a post-coronavirus stimulus plan, setting out a bold package of extra spending, tax cuts and help for business, worth €130bn, roughly 4% of German GDP.

Yet, again, this is not the extent of the good developments. On Thursday, the ECB fired a bazooka and confirmed that it would be increasing its so-called Pandemic Emergency Purchase Programme (PEPP) by €600bn to a total of €1.35tn. This was higher than analysts had expected.

Eurostoxx up 9%

The effect on markets was pronounced: the Eurostoxx 50 index was up 9% versus the S&P 500, which was up 2%. The Euro itself is appreciating handsomely and has risen 4% over the last two weeks. This provokes the question: who says markets are irrational?



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