

20 million reasons for caution

As Asia trades ahead of today's US jobs report, the idea of perhaps more than 20 million new jobless being priced into markets seems hard to accept



Go figure

I've long given up thinking that in some way, equity markets provide an insight into the economic future. Liquidity is the ultimate drug for equities, and the outlook for earnings seems to be of little real merit as a predictor.

But less than 24 hours ahead of what will probably rank as the "worst economic report in the history of the world" I find it puzzling that equity futures are hovering in slightly positive ground. [Check out this from James Knightley for more on the US jobs market.](#)

The usual excuse for this sort of thing is that all the bad news is already priced in. But if so, when did that happen? Recent equity market performance has been steady to slightly higher. And I don't believe that this point occurred the minute the S&P500 hit its 23 March bottom. Investors

were still talking about V-shaped recoveries back then (economists have been pretty clear - for once - that this was not on the cards from the word go - despite what you read in some sections of the media).

Could it in some way be a positive reaction to the fact that December Fed funds futures are now pointing to negative US policy rates? If so, they haven't been paying attention, because if this happens, the liquidity role played by US money markets would likely make financial conditions far tighter, rather than looser. And even in Europe, where liquidity is more of a bank function, negative rates have clearly not provided much help, and there is a good argument to suggest that they've done active harm.

Jerome Powell and his colleagues are smart and I don't think official Fed policy will ever go negative for these reasons. I don't rule this out for market rates further along the curve, however. But in short, the Fed has done practically everything of substance that you could have asked of them, so you can't reasonably put equity optimism down to stimulus expectations.

We'll see. For such a well-flagged car crash, the market reaction to this in either direction will be very interesting.

More trade worries next week

I read on the newswires that US and China trade negotiators will meet next week to see how China has been living up to the commitments that it made to secure last year's trade truce.

Very obviously, on a month by month basis, they will have fallen far short, thanks to the pandemic. But will the US make allowances for this? Reasonableness would argue, "yes". But the politics of this is not so clear. While there is little to be gained economically or in terms of market action from ripping the scab off this old wound, with the economic data flying off the charts in the wrong direction, it could make a useful diversion for the spin-doctors. Next week could also be quite "interesting" as a result.

Let inflation rise to 4%? What do you mean, let?

I skimmed over an article today that suggested that letting US inflation rise to 4% for a decade could help to wipe off the debt accumulated during the pandemic.

I'm sorry. "Let inflation rise to 4%?" Despite what were some of the tightest labour markets on record, and some of the correspondingly most accommodative monetary and fiscal policies on record, including trillions of dollars of quantitative easing, the US was barely able to hit its more modest 2% PCE inflation target for more than a few months in 2011, 2017 and 2018.

It's one thing to play with spreadsheets and "what if" scenarios. But this idea belongs in the trash can, along with the growing number of articles on stagflation I'm reading.

I'll be writing a longer, and most probably quite a ranty piece on why this is nonsense as soon as time allows. But the short version of the note would simply say - there is no mechanism for supply shortages to generate a cost-push inflation spiral any more. Growing alternatives to wage-labour (AI, automation), much larger service sector, decreased unionisation and collective bargaining, all mean that at worst, supply constraints lift the relative prices of a number of goods and services for a time. But it fails to generate the subsequent rounds that would cause this to stick, or to grow, irrespective of central bank accommodation.

No mechanism = no stagflation. Which is a pity, as in my view, as a bit of "flation" of any sort really would be quite useful. It's wishful thinking though. Debt write-downs are much more likely in my view.

Today in Asia

It is a quiet one today in Asia. Prakash Sakpal writes this on Malaysian industrial production and what it means for next week's GDP release: " March industrial production (IP) data today is the last element in our 1Q20 GDP estimate. We expect a 4.9% YoY IP fall, a negative swing from 5.8% growth in February as the Covid-19 lockdown starting in mid-March dented activity. This result would still deliver slightly positive quarterly IP growth. Both exports and manufacturing held their ground in 1Q, but were outweighed by a sharp slump in services due to stalled tourism and movement restrictions. We expect a 4.2% YoY GDP fall in 1Q20 (data is due next week, 13 May)".

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