

## 24 hours - a lot has changed

Yesterday evening, it didn't look as if there would be much to comment on today - but overnight - Fed to resume bond purchases, UK's PM Johnson gets Brexit snub from Merkel, and ahead of trade talks tomorrow sentiment sours.



Fed Chair, Jerome Powell

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### The big news, its QE in the US, or is it?

Overnight, US Fed Chair, Jerome Powell, has announced that the Fed would recommence outright Treasury asset purchases to try to calm the repo market, which has been beset by recent liquidity shortfalls and rate spikes.

It sounds as if the purchases will be made at the front end of the yield curve, unlike most QE operations, which were aimed at an average maturity of about 7 years (5 to 10-year maturity assets targeted).

What is interesting is just how vociferously Powell mentioned that this wasn't QE:

- "I want to emphasize that growth of our balance sheet for reserve purposes should in no way be confused with the large-scale asset purchase programs that we deployed after the financial crisis"
- In no sense is this QE", he added.

It is though, isn't it?

And all of this comes as the BIS, the Bank of International Settlements, the central bankers' bank, put out a report yesterday suggesting that the benefits of QE outweighed the costs. So, the institutions that undertook widescale QE, and in some cases, have re-opened the monetary spigots, have commissioned a report that says they did a good job? Why do I find that difficult to swallow?

[Here's a link to the report](#), chaired by RBA Governor, Philip Lowe. The RBA hasn't done QE, but at 75bp, the Australian cash rate is looking in danger of being replaced by unorthodox policies before long, despite apparently being on a gentle upturn. The last RBA 25bp rate cut earlier this month still takes some thinking about.

In a nutshell, the report says that while there may be some distortions to financial markets from such policies, on balance, they have been helpful, but would have been even more effective if coupled with more appropriate (expansionary) fiscal policies.

I can't help thinking that such policies are a bit like the monetary equivalent of opioid drugs. They were helpful in the depths of the financial crisis, when there literally was no other game in town, but their continued use and decreasing effectiveness, has left some central banks with a monetary "habit" that will prove very difficult to shake, and which sows the seeds for some very unfortunate and unintended (though perfectly forecastable) side effects. Widespread poverty in old age is one, not to mention increasing wealth inequality. I think their stimulative properties are also at best questionable, and potentially even the opposite to those intended.

New IMF Managing Director, Kristalina Georgieva, seems to take a more realistic view, and is apparently undertaking research looking at the pitfalls of negative interest rates. That should make very interesting reading when it is out.

Wow, and I didn't think there would be anything worth writing about when I went home last night!

## Trade optimism waning

The other overnight development is that optimism in some form of US-China trade deal, even a limited one, seems to be dimming. In some ways, this isn't surprising. The timing of the US travel bans and company blacklists associated with human rights issues have not helped to maintain a positive backdrop to these trade negotiations. They also look likely to provoke some retaliation from China, just a day before Vice Premier Liu He is due to arrive in Washington for trade talks.

While the US may insist that the two issues, trade, and human rights are separate issues, and indeed it is hard to argue against such a view, timing is everything. The latest developments cannot be reconciled as helping the prospects of a trade deal - no matter how limited in scope. Asian equity futures look fairly negative across the board today following a 1.56% fall in the S&P500 last night. US 10Y Treasury bond yields are heading lower again, and now only 1.53%, whilst the 2Y yield has taken a boost from the QE/not QE announcement and dropped to 1.419%.

A disappointing outcome to these trade talks would set up US Treasury yields to break past their September low of 1.4573%.

## Merkel to Johnson - "Nein!"

Angela Merkel has spelled out to PM Johnson that a deal with the UK that takes Northern Ireland out of the EU Customs Union is essentially impossible to achieve. Johnson is to meet Ireland's Prime Minister, Leo Varadkar, before the end of the week. But hopes for a deal look very poor.

Assuming that this does then prompt the PM to do as the Ben bill demands, which is to ask the EU for an Article 50 extension, and is then coupled with a quick election, this pitches the fate of Brexit into the hands of voters once more, albeit indirectly. Cable is a shade over 1.22 currently.

## China Monetary data due

Aggregate financing and new yuan loan data is due out later today. This is complicated data and there is little merit in pre-judging a report with so many moving parts. There is little else due out on the Asian calendar.

Last night, the US released its NFIB survey. This fell, reinforcing other recent softer macro releases. It does look as if the US economy is losing momentum. Our house forecast of an October rate cut followed by a further cut in December looks highly plausible given the recent run of data. It would get a further boost if trade talks come to nothing.

There is little of note from the G7 today.

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