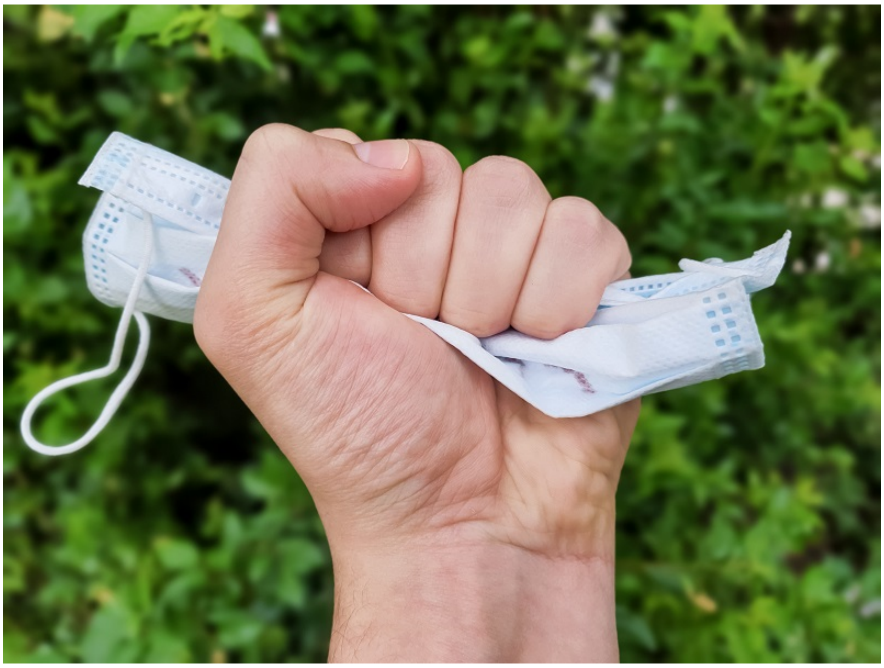
Curioser and curioser

President Trump's termination of talks on fiscal stimulus send stocks lower, dollar higher - an odd decision so close to the election



crushed mask

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Not what markets expected

I distinctly remember reading some analysis recently suggesting that President Trump's return to the White House would increase the chances of him pushing through a fiscal stimulus deal. Instead, within a short time of returning from hospital, he has called off talks, suggesting that the Democrats were not negotiating in good faith.

This is a curious decision. Dragging out the talks but reaching no satisfactory conclusion, President Trump could at least have claimed that the fault lay with the opposition. By unilaterally pulling the plug, at a time when many states are finding their ability to finance supplemental unemployment insurance challenged by lack of funds, this seems to be a gamble with a low probability of paying off, at least in terms of closing the polling gap with former Vice-President, Joe Biden.

Equity markets have responded negatively to the news, which in turn has spurred the dollar to gain against the EUR and also most of the currencies in our Asia Pacific region. Bonds have rallied slightly, with yields on the 10Y US Treasury bond backing down to just under 0.75%. Will this persist? Well, equity futures remain negative, though this often isn't much of a clue beyond the opening level for markets, and I'm not sure I would read too much into that.

Today (most likely tomorrow morning for those of us watching in Asia) VP Mike Pence will take on VP candidate, Karmala Harris. I'm hoping this will be a less "cringey" event than the first Presidential debate, which at times had me leaving the room to cope with the cringe-factor in a way that I haven't had to do since I watched Borat on a hotel pay per view. But as I mentioned before in this note, as far as markets are concerned, these debates, and especially the VP ones, are a sideshow. As for the election itself, there are probably no bad market outcomes except for a contested result. That comes back into play if Biden's lead starts to narrow, say below 7 percentage points, where the margin for polling error leaves the outcome less clear. With the lead remaining fairly steady currently, that isn't too much of a threat. Suggestions that a Democrat win might lead to an anti-trust investigation into the big tech giants might, however, see tech stocks beginning to give back some of their gains for the year. That could feed through into broader market weakness, so that's perhaps worth watching. Not a forecast though.

RBA's Lowe suggests stimulus to be maintained - not necessarily increased

Yesterday's RBA rate decision and statement by Governor Lowe don't really add a great deal to our thoughts on the Australian economy. The new Australian budget is announced later today, and some might have conjectured that a further element of monetary easing might be unveiled as a support to that. At a speech on 22nd September, Deputy Governor, Guy Debelle, outlined some of the additional measures that the RBA might take, of which the most likely were reducing the yield curve control target still further to 0.1% for the 3-year yield and the cash rate, and perhaps also going further along the yield curve in terms of asset purchases and targets. Negative rates were largely written off, as they continue to be in Lowe's latest statement, and rightly so in my opinion. I'm not supposed to make normative remarks, so let me say instead of saying that "negative rates are a bad policy", that "negative rates impact on economic activity is at best ambiguous, and in some cases could be outright negative". Regulations duly adhered to, let's return to Lowe's remarks, and the absence of any change to any aspect of monetary policy at yesterday's meeting.

I just don't think the Australian economy needs anything further right now. And I didn't find Lowe's comments particularly dovish. Instead, they appeared decidedly neutral, with all doors to further easing left open, but no particular indication that he is moving towards any of them. Lowe notes that the economy will continue to need monetary support for a substantial period. That's undoubtedly true. But I did not sense that he felt there was a need for additional incremental easing. Nonetheless, markets seem to be talking themselves into this. I very nearly caved and changed our forecast to reflect this, and indeed suggested so to our traders and sales this morning that I might do so. But on further reflection, and with the delayed help to my reasoning from several additional cups of tea, I don't see the reason for this as compelling, especially with the labour market continuing to make good progress and the Covid-19 problems of Victoria coming under control. So, the cash rate is more likely to stay where it is on reflection. Perhaps for a long time.

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