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QE FOR THE PEOPLE!

MACRO INSIGHTS

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Contents

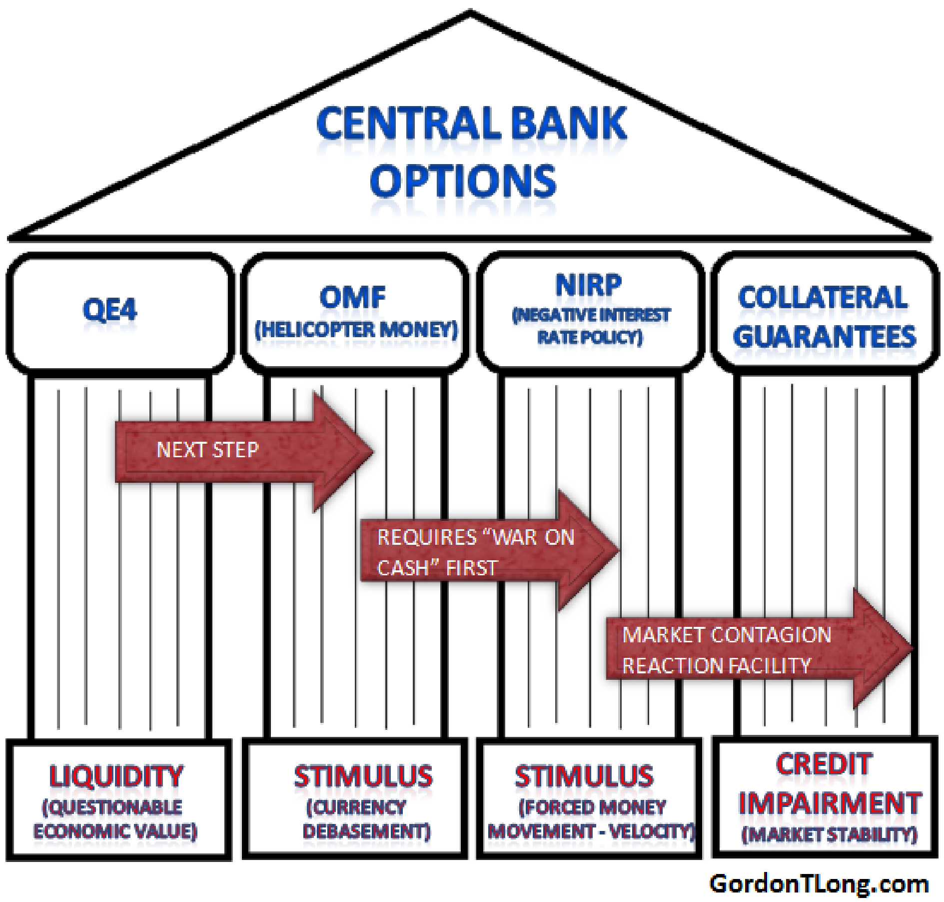
QE FOR THE PEOPLE!

WHAT ARE THE CENTRAL BANKERS' OPTIONS?

When a country consumes more than it produces for a sustained period of time, its Fiscal & Monetary choices will steadily decline.

We would argue slowly at first, then faster. Similar to US credit growth it is also exponential growth!

Because of this we believe the Federal Reserve and other developed economies' central banks will soon be forced to roll out, or unleash in a coordinated fashion, a number of new major policy initiatives to stem a potential global economic crisis.



In previous reports I have laid out that easy credit, quantitative easing and ZIRP has brought demand forward. More importantly, excess credit has fostered a massive global oversupply. Quantitative Easing is no longer bringing demand forward and in fact is now working against this by reducing Pricing Power and unleashing powerful global deflationary pressures. It is achieving the opposite of its original intended goals.

Moral Hazard and Unintended consequences have distorted the normal business cycle.

The capitalist system relies on the normal business cycle to keep it vibrant of functioning. Like trees in the forest, old trees must die to give way for new trees. When dead trees are not allowed to fall and thereby open up the sun's rays to new seedlings, a forest would die. Through rot and decay, nature takes care of this.

When 'well intentioned' public policies don't allow zombie and obsolete business to die, new businesses are not allowed to grow.

Today, through mistaken public policy we have "financialized" the economy to the point where it is killing growth due to lack of investment. Corporations are now incented into games of financial engineering, stock buybacks via cheap money and the avoidance of entrepreneurial risk. It is a natural consequence of sustained cheap money based on "unsound money".

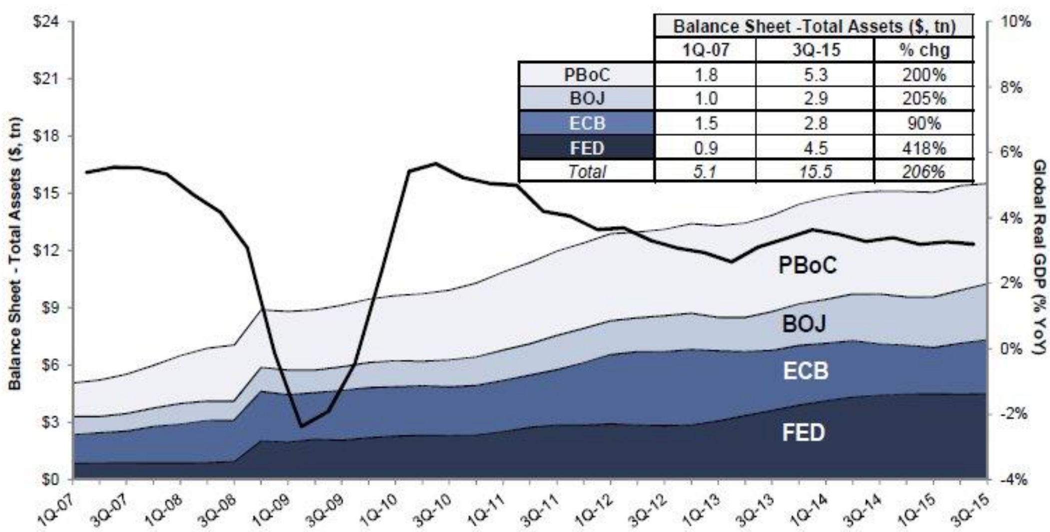
Inevitably, consumer "get less for more", instead of "more for less" which a functioning capitalist system will deliver.

"We now get less for more versus more for less!"

Since Q1 2007 central bank assets have grown by 206%. Meanwhile real Global GDP has been flat for the fourth straight year.

Exhibit 1: Despite Central Banks expanding their balance sheets, Global Real GDP growth has remained stagnant

Total assets on central bank balance sheets vs global real GDP (% YoY)

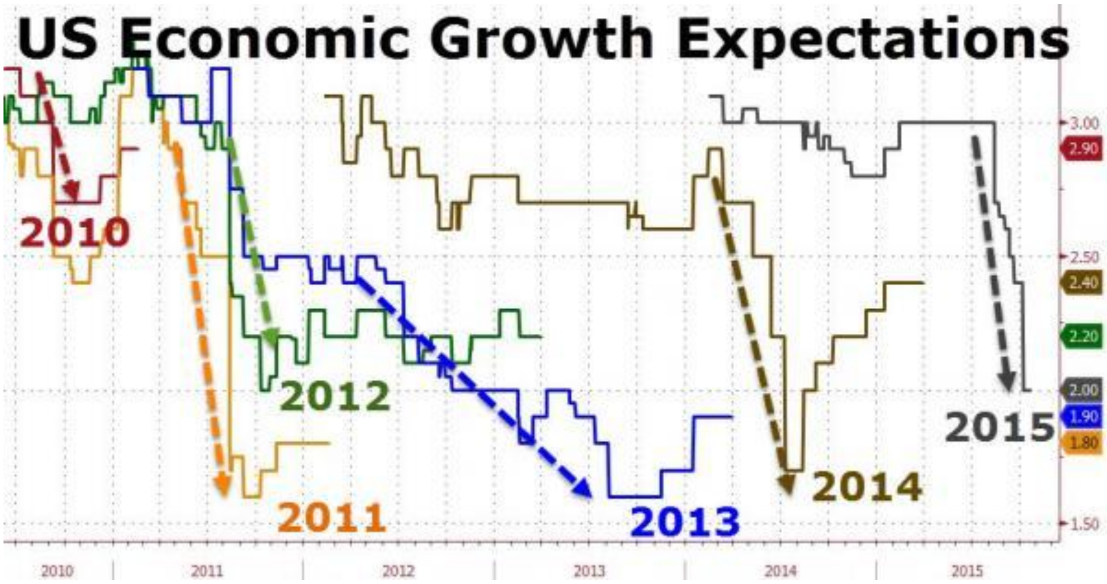


	Balance Sheet -Total Assets ($, tn)		
	1Q-07	3Q-15	% chg
PBoC	1.8	5.3	200%
BOJ	1.0	2.9	205%
ECB	1.5	2.8	90%
FED	0.9	4.5	418%
Total	*5.1*	*15.5*	*206%*

Note: Global GDP growth includes economies covered by GS Macro Research.

Source: Bloomberg, Goldman Sachs Global Investment Research.

What does this historical economic growth expectation comparison tells you? These are policy promises and expectations which were never delivered on. When do we finally question the economic path we have bneen following?



More and more are now talking about the complete failure of Quantitative Easing.

- *JAPAN*
  - *Japan's Problems Will Not Be Solved by More QE, RBS Warns*
  - *Japan Falls Into Recession for Second Time Under "Abenomics"*
- *ECB*
  - *ECB's Own Data Shows QE Program As Utter Failure, Largest Banks Dwindle, Depositor's Capital Eyed for Bail-Ins*
  - *Mario Draghi Admits Global QE Has Failed- -The Slowdown Is Probably Not Temporary*
  - *The ECB Should Stop QE Before Draghi Causes A -Financial Crisis-, German -Wise Men- Warn*
- *BOE*
  - *More QE Will Not Help the World – Fomer BOE Governor, Mervyn King*
- *FED*
  - *QE and ZIRP Failed... Will a Cash Ban Succeed?*
  - *Fed Admits -Something's Going On Here That We Maybe Don't Understand*
  - *Why The Fallacy Of The Fed's Feedback Loops Has Failed - -The Bust Is Still Underway*

Mainstream institutions are openly critical of what QE has wrought. Here is what RBS has to say about current central bank monetary policies with a preface from Tyler Durden

> As the global economy limps into 2016, the prospects for a sustained pickup in worldwide trade and/or a return to robust growth are decidedly grim.
>
> **Global trade growth has lagged the already tepid pace of global output expansion for three years running, averaging just 3% per year.** That's half of the rate witnessed from 1983 to 2008.
>
> Meanwhile, inflation expectations in developed economies have not rebounded, despite the best efforts of DM central bankers. And yet housing costs have soared in tandem with round after round of policy rate cuts and the global proliferation of QE, reflecting two things, i) central banks have learned nothing from the US housing bubble (that is, when you artificially suppress borrowing costs, housing prices soar), and ii) when you intentionally inflate bubbles in the assets most likely to be

concentrated in the hands of the wealthy (i.e. financial assets), those bubbles spill over into other asset classes like real estate and high end art.

What should be apparent from the above is that all the Mario Draghis and Haruhiko Kurodas of the world are doing at this point is blowing bubbles on the way to creating more inequality and embedding ever greater amounts of risk into capital markets not only by driving up prices, but by sucking out liquidity.

As for Main Street, there's no "wealth effect" (where "wealth effect" refers to a kind of neo-trickle down economics catalyzed by QE). There's only persistently slow growth, a jobs market that churns out more waiters and bartenders than it does breadwinner jobs, and a noticeably wider gap between the rich and the poor as exemplified by the fact that the billionaires of the world are paying $170 million for Modiglianis.

But the game is almost up. Central banks have monetized everything that isn't tied down. Hell, Kuroda owns half of the entire Japanese ETF market. Rates are below zero and there's only so much more NIRP banks are going to be able to stand before negative rates get passed on to depositors. Put simply: we're approaching the Keynesian endgame and there's still no growth, and no inflation (well, unless you count housing) and trade is collapsing.

Against this backdrop, RBS is out with 10 key points for 2016 and as you'll see below, **the overarching message is that the entire world is about to discover that the emperor(s) have no clothes.**

Note the last point (#10) as it, i) goes along with a previous note from Alberto Gallo in which RBS takes a close look at support for "radical" political parties in Europe (more on this here), and ii) makes a connection between recent economic outcomes in Europe, the ECB's evolving experience with ZIRP, NIRP, and QE, and Japan's lost decade.

* * *

From RBS

These are our key views for 2016:

1. **There are limits to monetary policy.** Central bankers will be tested in 2016. The economic equilibrium based on monetary stimulus, but lack of other measures is circular and fragile. Central bank balance sheets cannot grow indefinitely and forward guidance cannot target asset prices, without damaging credibility. Investors are growing increasingly wary of central bankers' credibility, and worried about the effectiveness of further stimulus (ECB, BoJ) and their ability to reverse policy (Fed, BoE).

2. **Fiscal stimulus, reforms and investment remain scarce.** The result is more QE in Europe and Japan, and a very shallow reversal of policy in the US and UK. We expect the ECB to deploy more QE in December, extending the length of the programme and the list of eligible assets. We think the BoJ will continue expanding its balance sheet as well. Conversely, exiting QE will be difficult even in the regions where it is deemed most successful – the US and UK – given lack of balance sheet deleveraging, or re-leveraging. Our economists expect the Fed to start hiking in December and to end at 1.5% at the end of 2016, with risks skewed to the dovish side, and the Bank of England to start hiking in August 2016. We think the impact of ECB QE2 will be temporary, as for QE1, due to persistent structural issues in the Eurozone economy. Despite convergence in periphery-core financial spreads, investment and loan volumes continue to decline, according to ECB data. The opportunity for US and European governments to build on the recovery is infrastructure investment and reforms, respectively. But what we are seeing is still too little, too late.

3. **More QE means central banks will own an increasing share of assets markets.** The ECB has already bought much of the free-float in European covered bonds, and the BoJ owns half of some stock ETFs in Japan. Without sovereign bond issuance, ECB QE demand will outpace bond supply by 2:1. This means the ECB will have to look for more assets (regional bonds, corporates), or that investors will be squeezed with lower yields or into other assets. However, given investment regulation, not every investor can move from asset to asset: some will have to learn to live with lower yields.

4. **Market liquidity will decline further, also due to central bank buying of assets.** This reduces both the free-float available, and the number of factors driving prices. Regulation will also continue to reduce dealers' ability to make markets.

5. China's top priority is reform, not stimulus: the slowdown will continue. A largescale stimulus is unlikely – instead, a long-series of reforms aimed at restructuring local governments, the financial sector, state-owned firms and at reducing corruption is what we are likely to see. If needed, Chinese policymakers have dry powder to smooth the landing, with cuts to the policy rate, bank reserve requirements or by using reserves. But the dry powder is not as much as it looks, compared to the length of the multi-year readjustment period for the Chinese economy.

6. **China-dependent economies will get hurt:** Brazil and Australia in particular. Brazil is the most vulnerable EM, on a combination of China exposure, dependence on $ debt, and political risk. Australia, still trading as a safe haven, is instead sitting on a very levered housing market and an export sector completely geared to China.

7. **Banks will need to live with low interest rates.** More disruption and consolidation is coming. This will challenge investment bank focused business models, and generally low-profitable banks. We see some opportunities from consolidation, e.g. in the Italian popolari. We are long, but avoid investment banks and EM-exposed banks.

8. Asset managers: **liquidity optimisation and bye bye to passive investing.** We see disruption in the asset management industry also. Passive strategies, IG in particular, will be replaced by ETFs. Active strategies will be increasingly detached from benchmarks. We look at liquidity optimisation as a way to build more efficient portfolios.

9. Deeper capital markets are part of the solution, but the solution is far away. A more flexible financial system, where debt restructuring is quicker and more efficient, could help economies to get out more quickly from a balance sheet recession. Despite the United Nations' call for a common framework for sovereign restructuring, Greek restructuring will continue to be a purely political decision and to be procrastinated.

10. **The equilibrium, for now, is QE infinity** – but political risk could be the breaking point. **Political risk could be the breaking point for the QE infinity equilibrium. Europe, unlike Japan, will not be able to go through a "lost decade" intact, given its political dynamics, elevated youth unemployment and rising radical parties.**

My Macro Analytics guest, Graham Summers writes that Even The Fed Admits QE Is a Failure:

Central Bankers will never openly admit that they or their policies have failed. Moreover, they do not rush into sudden tightening (more on this in a moment). But one can begin to notice subtle changes in their language and actions that indicate they have noticed what's happening in Japan (the failure of the BoJ's "shock and awe" QE program to generate growth).

Nowhere is this more clear than at the US's Federal Reserve or Fed. Indeed, starting in August 2013, various Fed officials began questioning the efficacy of QE.

First came the San Francisco Fed with a study revealing that QE generally doesn't appear to generate economic growth:

Asset purchase programs like QE2 appear to have, at best, moderate effects on economic growth and inflation*. Research suggests that the key reason these effects are limited is that bond market segmentation is small.*

Moreover, the magnitude of LSAP effects depends greatly on expectations for interest rate policy, but those effects are weaker and more uncertain than conventional interest rate policy. *This suggests that communication about the beginning of federal funds rate increases will have stronger effects than guidance about the end of asset purchases.*

http://www.frbsf.org/economic-research/publications/economic-letter/2013/august/large-scale-asset-purchase-stimulus-interest-rate/

A few months later, the former Fed official in charge of the Fed's first round of QE, penned a *Wall Street Journal* article stating that QE was in fact a Wall Street bailout.

I can only say: I'm sorry, America. As a former Federal Reserve official, I was responsible for executing the centerpiece program of the Fed's first plunge into the bond-buying experiment known as quantitative easing. ***The central bank continues to spin QE as a tool for helping Main Street. But I've come to recognize the program for what it really is: the greatest backdoor Wall Street bailout of all time…***

It wasn't long before my old doubts resurfaced. Despite the Fed's rhetoric, my program [QE] wasn't helping to make credit any more accessible for the average American*. The banks were only issuing fewer and fewer loans. More insidiously, whatever credit they were extending wasn't getting much cheaper. QE may have been driving down the wholesale cost for banks to make loans, but Wall Street was pocketing most of the extra cash.*

http://online.wsj.com/news/articles/SB10001424052702303763804579183680751473884

Around this time, the Fed began to taper QE first by $10 billion in December… and another $10 billion in January. By this point even uber-dove Fed President Bill Dudley (he formerly claimed inflation is low because iPads are getting cheaper) even admitted the following:

We don't understand fully how large-scale asset purchase programs work to ease financial market conditions*—is it the effect of the purchases on the portfolios of private investors, or alternatively is the major channel one of signaling?*

http://www.ny.frb.org/newsevents/speeches/2014/dud140104.html

At this point, Ben Bernanke handed off the reins for Fed Chairman to Janet Yellen. Yellen has since continued Bernanke's tapering projects, reducing the monthly QE spend from $65 billion to $55 billion.

The failure of the Bank of Japan's massive QE program and the Fed's decision to taper are not unrelated. Take a look at the timeline.

- April 2013: Japan announces a "shock and awe" QE program.
- August 2013: San Francisco Fed economists (where future Chairman of the Fed Janet Yellen is President) write a study showing QE is ineffective at generating economic growth.
- November 2013: Former Fed officials admit QE was not meant to help Main Street.
- December 2013: the Fed begins to taper its QE programs by $10 billion
- January 2014: Bernanke's last FOMC as Fed Chairman, Fed announces another $10 billion taper
- March 2014: Janet Yellen takes over at the Fed and announces *another* $10 billion QE taper.

This represents a tectonic shift in the financial markets. It does not mean that Central Banks will never engage in QE again. But it does show that they are increasingly aware that QE is no longer the "be all, end all" for monetary policy.

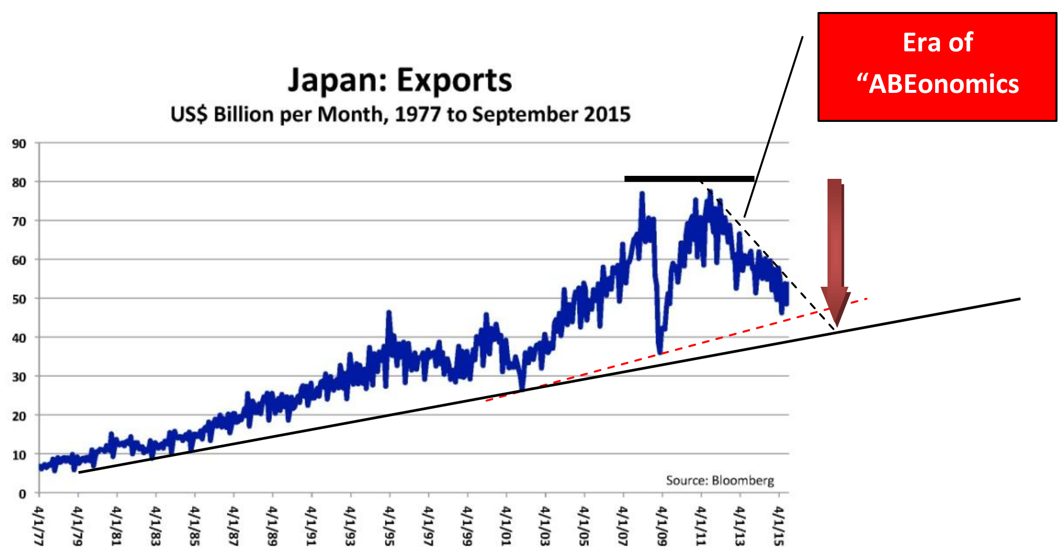
Investors take note. One of the primary market props of the last five years is being removed. What happens when the markets finally catch on?

JAPAN HAS SHOWN US QE DOESN'T WORK – *More Than Enough Proof!*

- *Japan's Problems Will Not Be Solved by More QE, RBS Warns*
- *Japan Falls Into Recession for Second Time Under "Abenomics"*

IT'S ALL A SHAME AND PROPAGANDA!

Read below and see if you can spot the "touchdown"?



Japan's Problems Will Not Be Solved By More QE, RBS Warns

One thing that became abundantly clear about QE long ago even if it hasn't yet dawned on Mario Draghi or Haruhiko Kuroda, is that the practice of monetizing anything and everything that isn't tied down (or that you can't pry from the cold dead hand of an institutional investor), **is subject to the law of diminishing returns.**

Put simply: eventually it just stops working in terms of stimulating aggregate demand and/or boosting growth and inflation expectations.

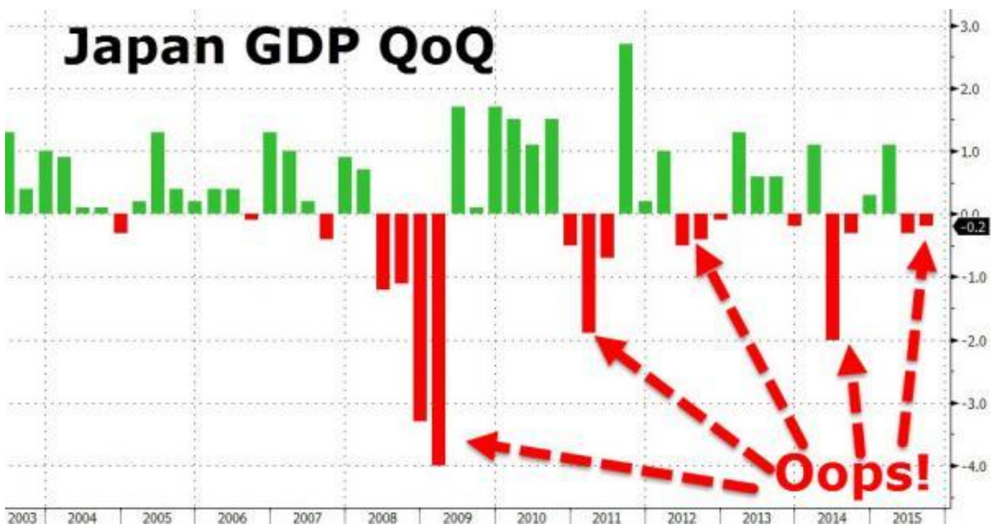
Unfortunately, the deleterious effects of QE are *not* subject to the same dynamic.

That is, when you print another say, €750 million to monetize everything from periphery EGBs to SSAs to munis, you invariably impair market liquidity on the way to creating the conditions for dangerous bouts of volatility (see the great bund VaR shock for instance).

Of course when you go full-Kuroda and simply corner the market for ETFs by stepping in to provide plunge protection at the first sign of Nikkei weakness, there's no telling what kind of chaos you've set everyone up for once you step out of the market. Meanwhile, the mad dash to inflate the value of stocks and bonds has served to create enormous bubbles not only in those assets, but also in the things people who hold those assets are likely to buy when they get bored - like real estate and high end art.

In short, the drug addiction analogy (as cliche as it now is) still holds up remarkably well. For a drug addict, the benefits (i.e. the high) diminishes the more the addiction grows, but the harmful effects on the body do not. **It's the same thing with QE. The initial "high" wears off, but the asset bubbles only grow.**

Nowhere is this more apparent than in Japan where just last night, we witnessed the unprecedented "quintuple recession":



As if that wasn't bad enough, **Japanese business spending dropped 1.3% QoQ - its worst drop since Q2 2014.**

Of course the Nikkei is doing just fine, surging right alongside the BoJ's balance sheet.

In honor of Kuroda and his special brand of Peter Pan-inspired, neo-Keynesian madness, we present a bit of color from RBS' Alberto Gallo on Japan and QQE.:

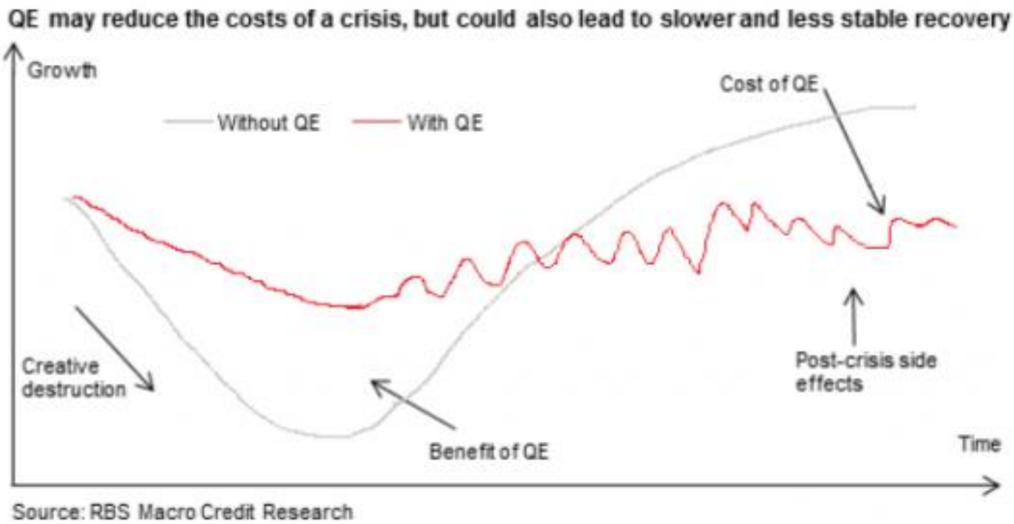
QE infinity? *Japan re-enters into recession; the Economy Minister suggests that labour unions are still stuck in a deflationary mind-set. The Japanese economy suffered a technical recession again in Q3, contracting -0.8% QoQ on an annualised basis, following a -0.7% drop in Q2.*

Inflation has also fallen back again, reaching 0% in September (below). One major reason for this is weak wage growth.

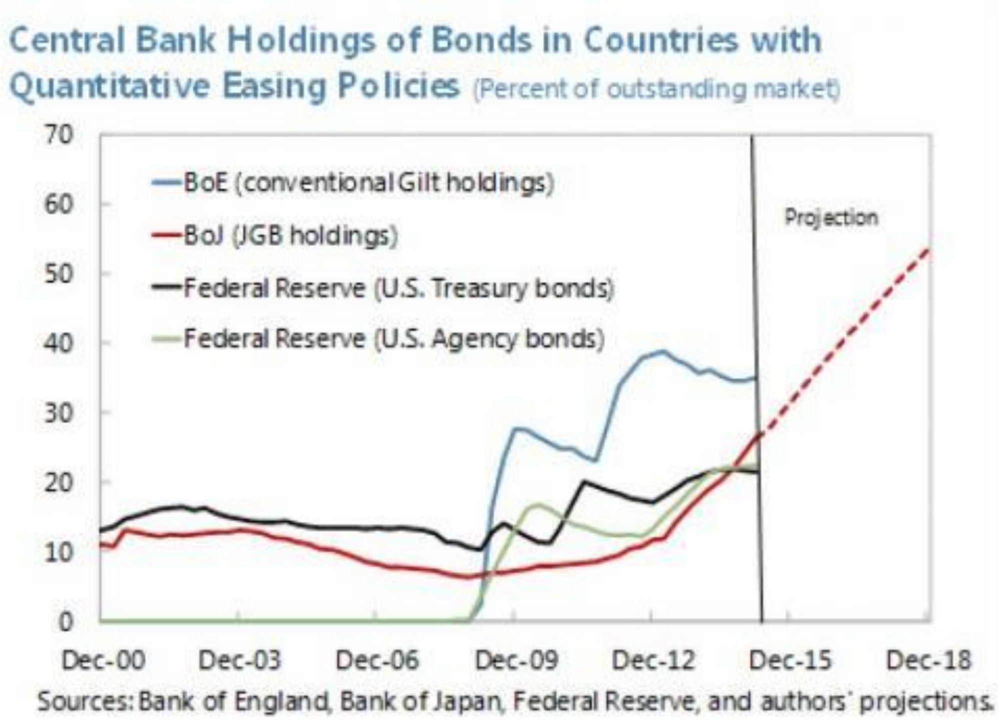
Why has QQE failed to boost growth and inflation for Japan? Cyclical tools are insufficient to tackle the country's structural issues. *Japan's problem started in the 1980s, when firms increased debt by 14% of GDP per year to reach 130% of GDP by 1995 (BoJ). This was followed by two decades of slow corporate deleveraging, deflation/weak inflation, near-zero interest rates and compressed bond yields, albeit with few bond defaults. Under PM Abe, the Bank of Japan has stepped up monetary easing by initiating the Quantitative and Qualitative Easing (QQE) programme in April 2013 and expanding it in October 2014.*

However, the issues faced by Japan are more structural, including an ageing population, low investment appetite for corporates and a widespread deflationary mindset as suggested by Amari.

*Japan's experience suggests that **QE has its limits, and could bring a range of side effects**, in our view. **These include years of tepid growth (see below), the reduction in secondary trading liquidity, an increase in asset ownership by central banks (the BoJ now owns half of the national ETF market), potential formation of asset bubbles and social problems like inequality.***



Ok, so in other words: Kuroda isn't going to be able cure the country's structural problems which include the well worn issue of Japanese demographics as well the much maligned "deflationary mindset" which seems largely immune to the hum of the BoJ's prinitng press. Nevertheless, Japan is all-in and is apparently prepared to keep the pedal to the floor until 2018 when, as we've documented extensively, the game will officially be up (see [here for instance](#)).



In the meantime, as Gallo rightly points out, you can expect an impaired secondary market for JGBs, asset bubbles, and rising inequality (all outcomes we've discussed at great length) as Kuroda triples, quadruples, and quintuples down on policies that now seem to be producing around one recession per QE iteration.

Bloomberg

Japan Falls into Recession for Second Time Under 'Abenomics'

- Japan Needs 'Aggressive' Structural Reforms: Boubouras
- GDP data shows slumping business investment hurt the economy
- Report could put pressure on Abe, BOJ's Kuroda for action

Japan's economy contracted in the third quarter as business investment fell, confirming what many economists had predicted: The nation fell into its second recession since Prime Minister Shinzo Abe took office in December 2012.

Gross domestic product declined an annualized 0.8 percent in the three months ended Sept. 30, following a revised 0.7 percent drop in the second quarter, meeting the common definition of a recession. Economists had estimated a 0.2 percent decline for the third quarter.

Weakness in business investment and shrinking inventories drove the contraction as slow growth in China and a weak global outlook prompted Japanese companies to hold back on spending and production. While growth is expected to pick up in the current quarter, the GDP report could put pressure on Abe and Bank of Japan Governor Haruhiko Kuroda to boost fiscal and monetary stimulus. The BOJ holds a policy meeting later this week.

"This report shows the increasing risk that Japan's economy will continue its lackluster performance," said Atsushi Takeda, an economist at Itochu Corp. in Tokyo."The weakness in capital spending is becoming a bigger concern. Even though their plans are solid, companies aren't confident about the resilience of economy at home and abroad."

- Inventories subtracted 0.5 percentage point from growth this quarter as companies reduced stocks that had expanded over the previous two quarters, the Cabinet Office said.
- Business investment subtracted 0.2 percentage point from growth.
- Private consumption added 0.3 percentage point of growth.

The reduced investment is a rebuff for Abe, who called on Japanese companies to put more of their record cash holdings into capital spending. From the previous quarter, business investment fell 1.3

percent in the July-September period, following a revised 1.2 percent contraction, according to the report.

Abe has made bolstering the economy a priority and advocated for reflationary policies that weakened the yen and boosted corporate profits. Kuroda had said in September it wouldn't be unusual for the economy to grow in the July-September quarter.

Bank of Japan officials didn't see the GDP report as likely to change their outlook for an improving trend in inflation, people familiar with discussions at the central bank said last week.

Hiroaki Muto, chief economist at Tokai Tokyo Research Center Co., said that while he thinks the economy "might have hit the bottom" in the third quarter, there's a strong chance that the government will compile an economic package to shore up growth.

Yen Strengthens

The yen strengthened after the data was announced and was up 0.1 percent at 122.52 per dollar at 11:50 a.m. in Tokyo. Investors have purchased the yen as a haven following the terrorist attacks in Paris. The Topix stock index dropped 0.8 percent in the morning session amid a broad-based decline in Asian share markets.

In a string of somber economic reports in the past few months, Kuroda's core price gauge fell, household spending unexpectedly dropped, vehicle production declined, retail sales slipped and imports fell while exports stagnated. One bright spot: Industrial output advanced 1.1 percent in September from the previous month, yet wasn't enough to make up for contractions in July and August.

"The BOJ should act now if they are looking at economic fundamentals: prices are falling and economy isn't growing, giving no sign for inflation expectations to rise," said Itochu's Takeda. "As for the question of whether they will act, it's hard to say."

Economy Minister

Abe has told Economy Minister Akira Amari to compile measures this month to help achieve his goal of expanding Japan's nominal GDP by 20 percent to 600 trillion yen over five years.

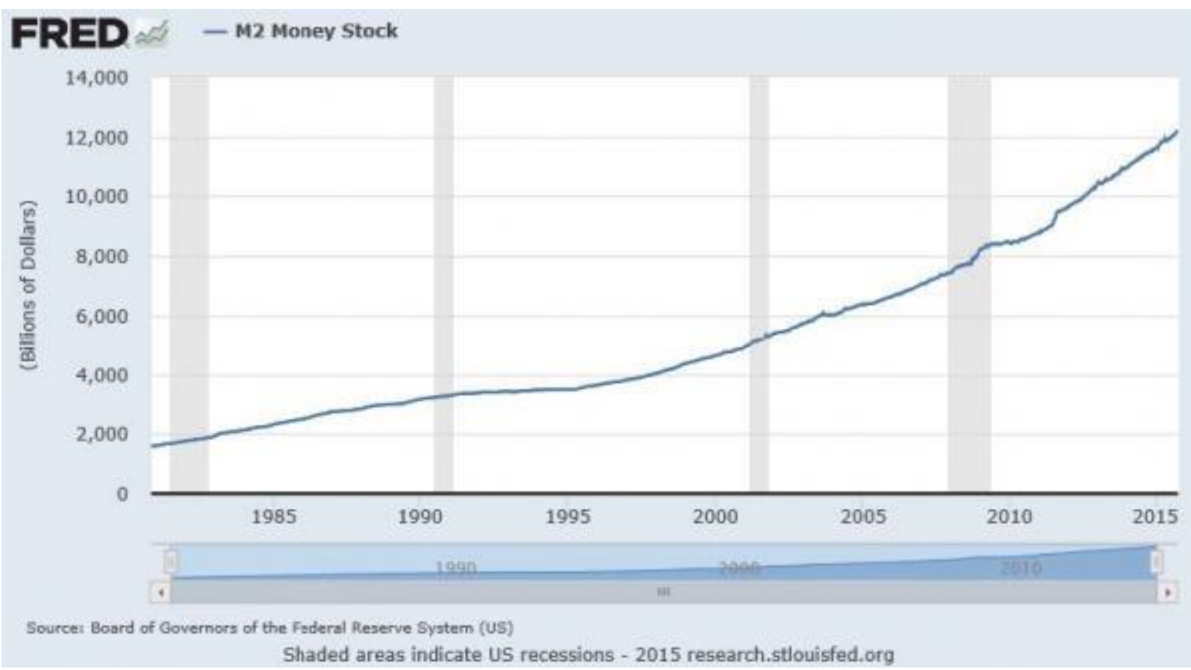
Amari said Monday after the data that an extra budget may focus on addressing Japan's demographic issues and to help alleviate the effects of the Trans Pacific Partnership trade pact and the government would take a flexible approach to fiscal and economic management. Amari also said GDP was likely expand in the current quarter.

WHAT THEY THINK NEEDS TO BE DONE

Further Expansion of the Central Bank Balance Sheets

According to the Fed, there is about $60 trillion of US Dollar credit (claims for US dollars):

Also according to the Fed, there are about $12 trillion US dollars:



So, the data show plainly there are five times as many claims for US dollars as US dollars in existence. Does this matter to investors? According to [Paul Brodsky](#) Macro Allocation it certainly does:

> *"The value of dollar-denominated assets is not supported by the money with which it is ostensibly valued. This has not been a problem historically because the proportion of un-reserved credit has been low relative to asset values and cash flow. As we are seeing today, however, it is becoming a significant problem because balance sheets are already highly levered and zero-bound interest rates chokes off the incentive to refinance asset prices higher.*
>
> *If the total value of US denominated assets is, say, $100 trillion, and the US dollar money stock is somewhere around $12 trillion, then the inescapable implication is that the market's expects either: a) $88 trillion more US dollars will be created in the future to fund the purchase of the gross asset pool at current valuations; b) there has to be a decline in the nominal value of aggregate assets, or; c) both.Obviously there never has to be a full exchange of assets for money because there will always be asset holders wishing to keep their assets. But that is not the point. The issue is that there is a significant rate of inflation embedded in the currency (clearly higher than 2% targeted by the Fed), and/or a significant rate of deflation embedded in assets.*
>
> *What forces the issue? Production, or the lack thereof. If/when the value of asset prices exceed the value of production by an amount that disincentives production, GDP will contract.*

Brodsky further argues:

"Either the Fed and other central banks overseeing highly leveraged economies must:

1. Inflate their money stocks and get the new money into the hands of debtors, or
2. Inflate their money stocks and get the new money to creditors.

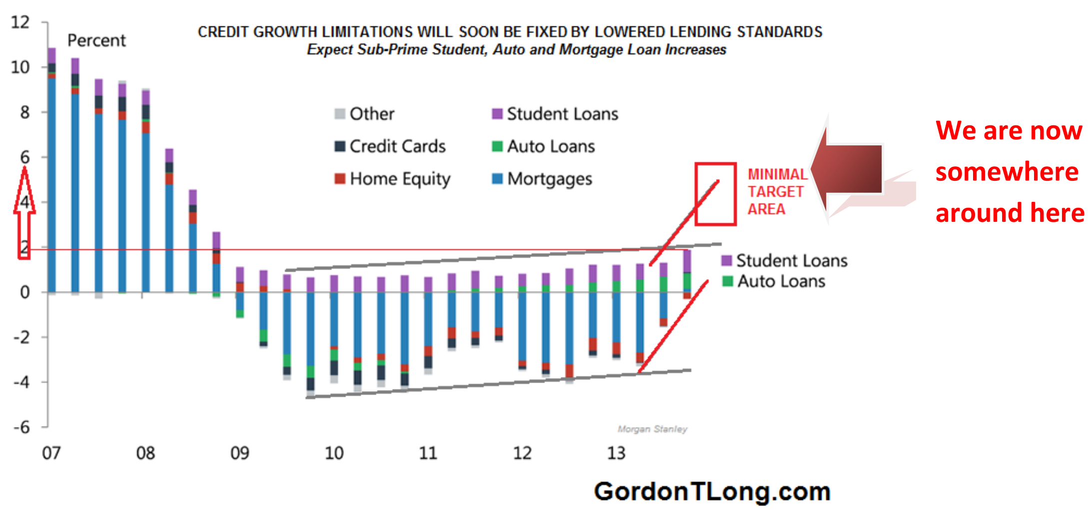
The former would make systemic debt service and repayment easier. The economic impact of getting new money in the hands of debtors would be significant inflation.

The latter would keep creditors solvent when debtors inevitably default. The economic impact of creating more bank reserves would be significant economic austerity (a full-blown depression). Why? Because debtors would be increasingly starved of the ability to service and repay debt."

Shadow Banking & Securitization Won't Carry the Day

I showed this chart a couple of years ago and argued that the government and its regulators had little choice following the 2008 financial crisis but to force growth by any means in both student loans and auto sales.

It has succeeded, but at what cost and systemic risk?

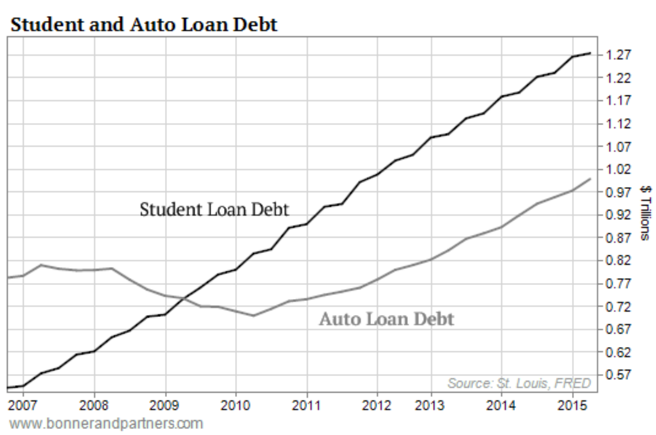


Both are dependent on the Shadow Banking system for their survival and growth. In the case of the auto industry for ABS (Asset Backed Securities) and in the case of student loans for Sallie Mae and it's financing through the shadow banking industry. It was MBS (Mortgage Backed Securities) that was the central problem in the 2008 crisis. The only thing that has changed is the vehicles and acronyms which justify them. We have talked about this before.

Credit based spending has been in full effect with auto loans and student debt since not long after the 2008 financial crisis. With so many creditworthy Americans deep in debt, the temptation has been to go to subprime loans, which have accelerated dramatically.

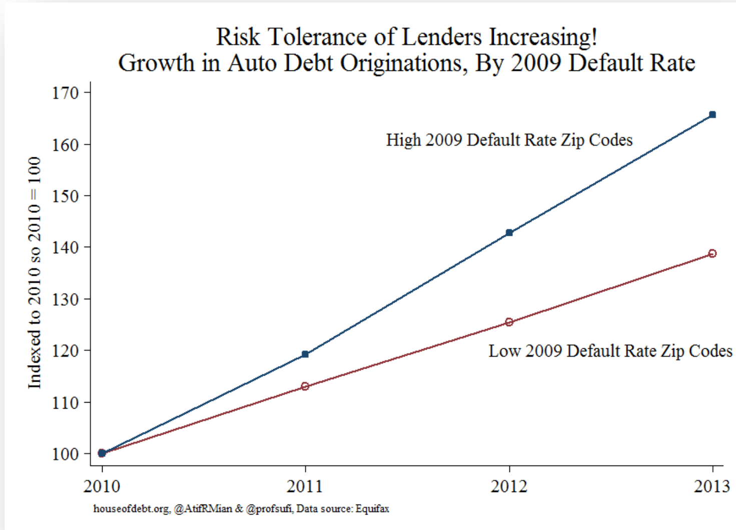
Subprime auto debt is running rampant. Student debt is now the most delinquent debt class in America. Subprime debt is once again super charging the debt fueled market. **Subprime debt is back in a big way**

Over the last seven years courtesy of the Fed's low rate policies, auto and student debt has surged in dramatic fashion. While the shrinking middle class is unable to purchase homes with inflated values, many are still chasing the dream by going into debt for cars and college. The debt growth in these markets can be seen to be nothing short of fantastic.

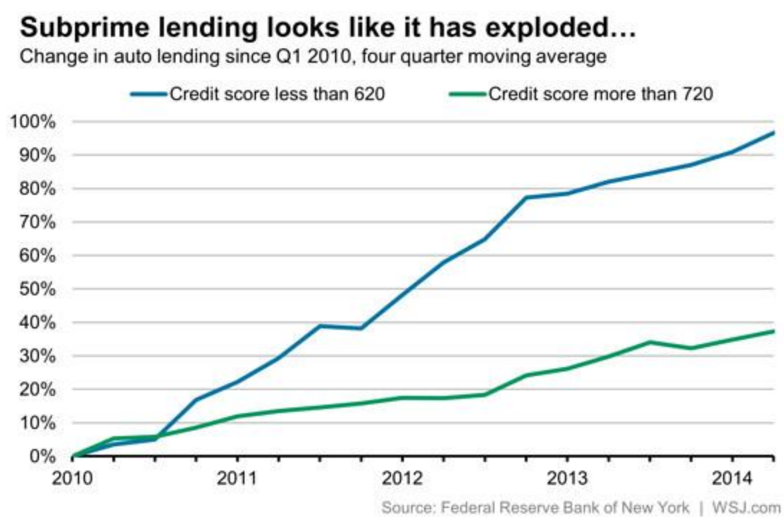


This is obviously the direct result of low interest rates and resulting consumer spending. We've essentially allowed Americans to buy cars on borrowed money and go to college on big debt while making it tougher for them to purchase homes based on the last crisis. Like wars, we always fight the last war with weapons that are obsolete in facing the new war.

What is scarier about this sudden growth is that much of the debt is being made to people that are having a difficult time paying it back. Take a look at subprime auto debt shown here.



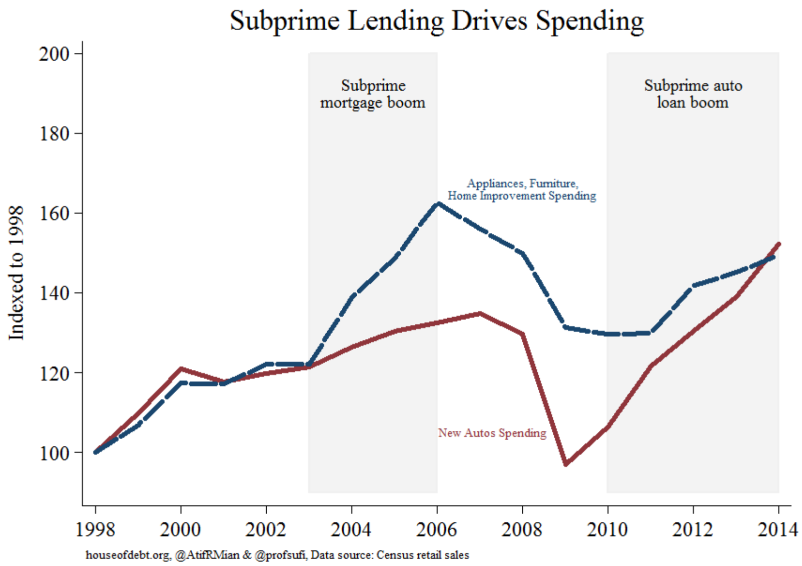
For auto loans since 2010 the growth in lending has come to consumers with credit scores of 620 or less. Those with higher credit scores of 720 have seen modest growth. Those with lower scores have seen nearly a 100 percent increase in loans while those with better scores have seen less than a 40 percent increase. In other words, the bulk of new cars are being bought with financing with those having trouble managing their current debt.



With cars costing $30,000 and higher, this is no small price tag. Any tiny little hiccup in the economy and this is enough to send their auto purchase into repossession. Do people remember the cash for clunkers and auto industry bailouts? These things did not happen too long ago. It appears that we are setting ourselves up perfectly for another kind of these scenarios.

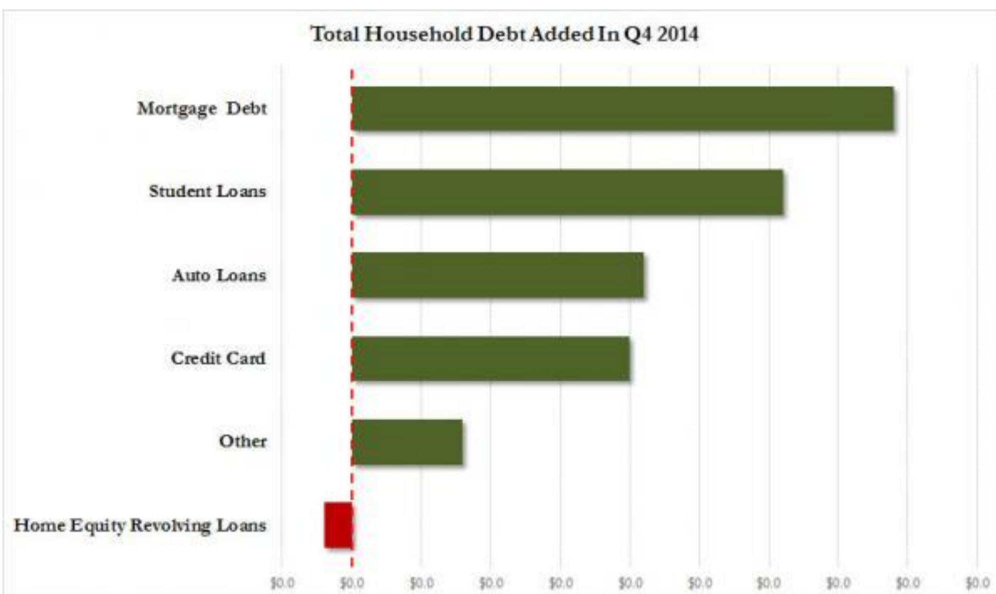
The results of prolonged artificially low rates is that the market is now fully addicted to this environment.

The Fed is backed into a corner and they really have very little ammo left. Speculative lending is already dominating the market. You can see the subprime booms very clearly.

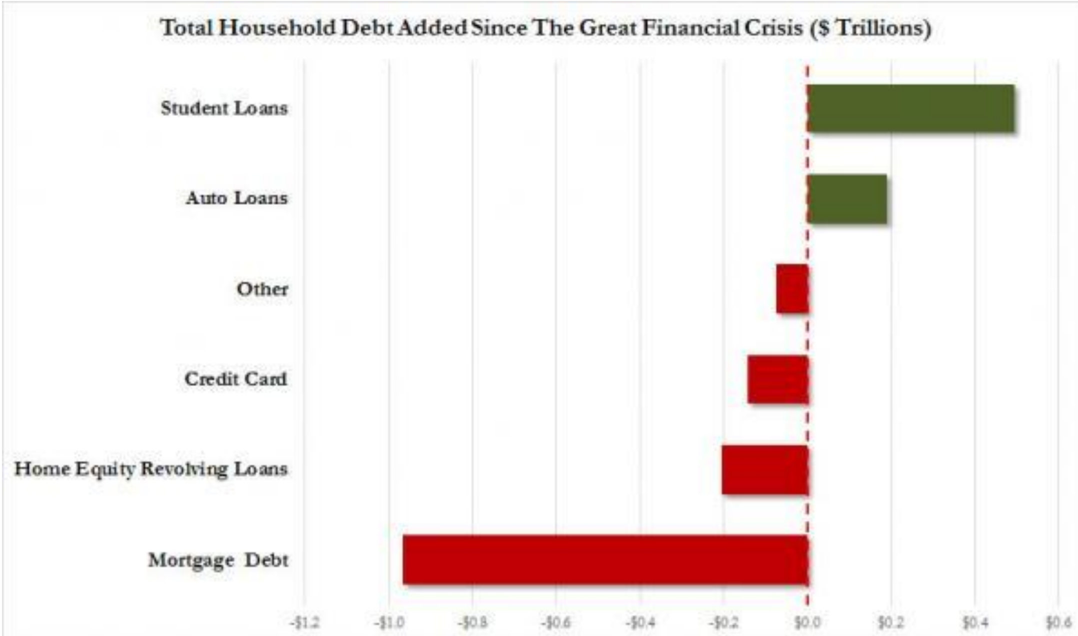


The economy is clearly slowing down. Recessions happen. And once again we have saddled a large enough group of Americans with debt where the pain will be deeply felt when the correction hits again.

Total household debt has continued to grow!

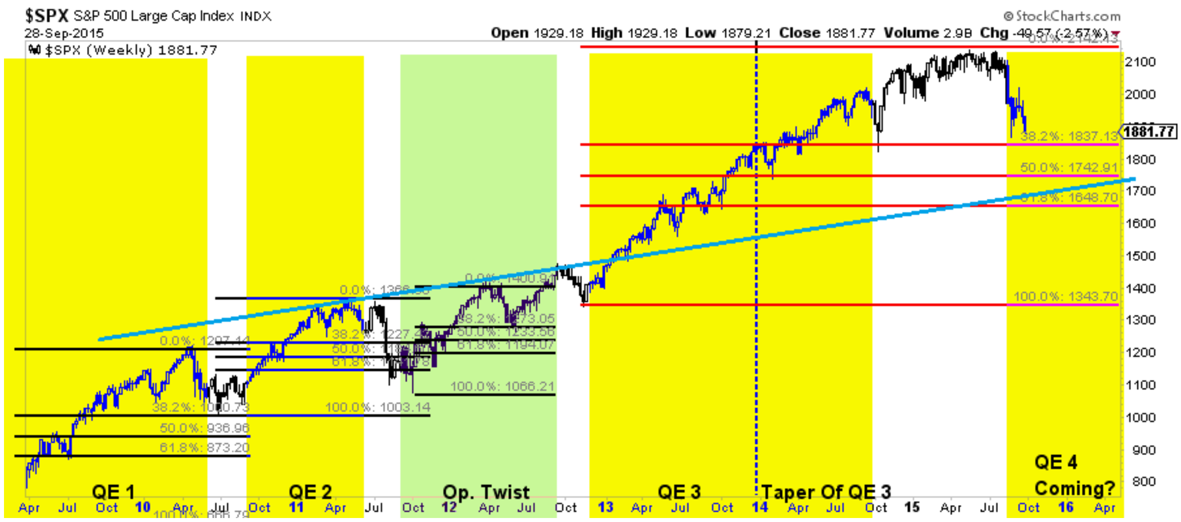


Total household debt added since the great financial crisis has been primarily in student loans and auto loans.

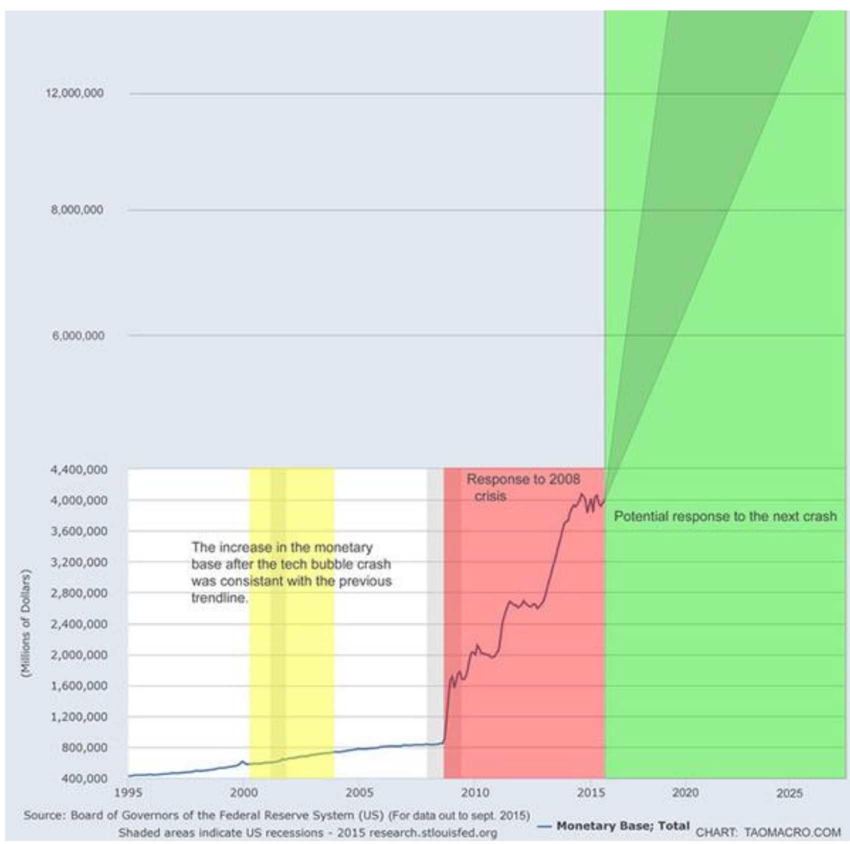


A huge difference between now and 2008 is that the US consumer is tapped out, the US middle class not making a "living wage" and debt being the only way for them to survive. Debt they have almost no ability to pay off! Credit has become a charade to postpone the inevitable.

My friend Richard Duncan has laid out in Macro Watch that there is insufficient Credit growth occurring in the US which results in a recession if not soon corrected.



What we can expect is shown in dark green.



OMF – *"Helicopter Money"*

Here is a sampling of what is appearing in the media as the conditioning of public opinion begins.

- A Stunning Admission From A BOE Central Banker- This Is What The Coming -Helicopter Money- What it Will Look Like

  Back in early 2009, just around the time the Fed announced it would unleash QE1, we warned that any attempt to reflate the debt (a pathway which ultimately leads to hyperinflation as monetary paradrops are the only logical outcome as a result of the deflationary failure of the intermediate steps) would fail, and instead would saddle the world with even more debt, making monetary financing, i.e.,*paradropping money*, the inevitable outcome.

  We said that instead, the right move would be to liquidate the excess debt, and start anew - a step which, however, would wipe out trillions in (underwater) equity, something which the status quo would never agree to, as that is where the bulk of its wealth is contained.

  7 years later, debt is well over $200 trillion, having risen by more than $60 trillion in the interim, and we are rapidly approaching the peak of the world's debt capacity as we noted a month ago in "The World Hits Its Credit Limit, And The Debt Market Is Starting To Realize That."

  Today, we find that none other than Adair Turner, a *member of the Bank of England's Financial Policy Committee* and a Chairman of the Financial Services Authority, wrote a long essay in Bloomberg which admits **everything** we have warned about.

  To wit:

  > *Advanced economies' public debt on average increased by 34 percent of GDP between 2007 and 2014.* ***More important, national incomes and living standards in many countries are 10 percent or more below where they could have been, and are likely to remain there in perpetuity.***
  >
  > ***The fundamental problem is that modern financial systems inevitably create debt in excessive quantities****. The debt they create doesn't finance new capital investment but the purchase of existing assets, and above all real estate. Debt drives booms and financial busts.* ***<u>And it is a debt overhang from the last boom that explains why recovery from the 2007–2008 crisis has been so anemic.</u>***
  >
  > *... debt contracts also have adverse consequences: They're likely to be created in excessive quantities. And the more debt an economy assumes, the less stable that economy will be. The dangers of excessive debt creation are magnified by the existence of banks and the predominance of certain kinds of lending. Almost any economics or finance textbook will describe how banks take money from savers and lend it to borrowers, allocating money among investment options.*
  >
  > *At the core of financial instability in modern economies lies this interaction between the infinite capacity of banks to create new credit, money and purchasing power, and the scarce supply of urban land. Self-reinforcing cycles of boom and bust are the inevitable result.*

  His punchline: "**unless tightly constrained by public policy, banks make economies unstable**."

  > *If central banks increased interest rates to slow the credit growth, standard economic theory said lower real growth would result. The same pattern and the same policy assumptions can now be seen in many emerging economies, including China:* ***Each year, credit grows faster than GDP so that leverage rises and credit growth drives economies forward.***

  And then this:

  > *But if that is really true, we face a severe dilemma.* ***We seem to need credit to grow faster than GDP to keep economies growing at a reasonable rate, which leads inevitably to crisis, recession and debt overhang. We seem condemned to instability in an economy incapable of balanced growth with stable leverage.***

Hmm, this sounds exactly like what we said in 2010: "Why The Staggering U.S. Debt Load Is Sure To Prevent Economic Growth." But what does a fringe, tin-foil blog know.

So, yes, the very top echelon of central bankers finally admits what we have said all along: creating excess debt creates asset bubbles, slows down growth, recurring crises and leads to even more "unconventional", and taxpayer funded systemic bailouts.

Hardly a surprise.

What does Turner recommend?

For the answer we have to go back to what he said yesterday in an IMF paper titled "The Case for Monetary Finance – An Essentially Political Issue." But before going into it, here is what the WSJ reported the IMF new chief economist, Maurice Obstefld, said:

> *"I worry about deflation globally," new IMF Economic Counselor Maurice Obstfeld said in an interview ahead of an annual IMF research conference that focuses this year on unconventional monetary policies and exchange rate regimes.* ***"It may be time to start thinking outside the box."***
>
> *Weak—and in some cases falling—price growth has plagued Japan, Europe, the U.S. and other major economies since the financial crisis. Plummeting commodity prices are exacerbating the so-called "lowflation" and deflation problems that curb investment, spending and growth.*
>
> *Surveying several dozen of the largest economies around the world, Mr. Obstfeld said the number of countries experiencing low inflation is rising. Combined with slowing emerging market output, ballooning government debt and monetary policy constrained by the lower limits of interest rates,* ***the deflation risk is fueling fears the global economy could be fast stuck into a deep low-growth mire.***

Yes, this comes as the Fed is desperately pushing for a rate hike, just so it can telegraph that "things are better than they seem." It remains to be seen how successful this experiment will be: we know that every single country that has been at ZIRP or below, and has tried to hike rates, has promptly failed most notably the case of Japan in August 2000 when it, too, hiked by 25 bps from 0% only to lower 7 months later.

Which brings us back to Adair Turner, and his note on "monetary financing." This is what he says:

> *"Monetary finance" is defined as running a fiscal deficit (or a higher deficit than would otherwise be the case) which is not financed by the issue of interest-bearing debt, but by an increase in the monetary base – i.e. of the irredeemable fiat non-interest-bearing monetary liabilities of the government/central bank.*
>
> ***The easiest way to think about this is in terms of Friedman's "helicopter money****", [Friedman, M. 1960] with the government printing dollar bills and then using them to make a lump-sum payment to citizens.*
>
> *But in modern reality:*
>
> - *It could involve either a tax cut or a public expenditure increase which would not otherwise occur.*
> - *It can be one-off or repeated over time.*
> - *And it would typically involve the creation of additional deposit rather than paper money. This would be initially in the form of deposit money in the government's own current accounts which would then be transferred into private deposit accounts either as a tax cut or through additional public expenditure.*

And the punchline: this is what the upcoming monetary paradrop will look like:

> *There are a number of ways in which the money could be "created" with different precise implications for the central bank balance sheet. They include:*

- ***The central bank directly credits the government current account (held either at the central bank itself or at a commercial bank) and records as an asset a non-interest-bearing non-redeemable "due from government" receivable***
- ***The government issues interest-bearing debt which the central bank purchases and which is then converted to a non-interest-bearing non-redeemable "due from government" asset***
- ***The government issues interest-bearing debt, which the central bank purchases , holds and perpetually rolls over (buying new government debt whenever the government repays old debt), returning to the government as profit the interest income it receives from the government. In this case the central bank must also credibly commit in advance to this perpetual rollover.***

But the choice between these different precise mechanisms has no substantive economic consequences, since in all cases:

- *The consolidated balance sheet of the government and central bank together is the same.*
- *The monetary base of irredeemable non-interest-bearing money is increased*
- *And the government is thus able to cut taxes or increase expenditure without incurring any future liability to pay more interest, or to redeem the capital value of the money created.*

And so on: there is more in the paper which we suggest everybody reads as it lays out precisely what will happen once the next attempt to reflate fails.

What is more disturbing, is that this is now effectively policy: with this paper by one of the most respected economists among the intellectual oligarchy, which expressly endorses "monetary financing" it is just a matter of time before it goes from theory to practice, first in Japan ***within the next five years***. Quote Turner:

> ***Monetary finance in today's economic circumstances.*** *I argue that monetary finance should be an available policy tool, and that in at least one country – Japan - it not only should be but inevitably will be used* ***within the next five years****.*

First in Japan, then everywhere else and... on a "***continuous basis.***"

> *I also consider whether money finance should be used only as an emergency measure in the face of a post-crisis debt overhang, or whether, faced with possible secular stagnation,* ***we will have to use it on a continuous basis.***

So the blueprint for what is coming has now been laid out and only those who willingly refuse to see what is before them, will be surprised when "monetary financing" is finally unveiled.

In conclusion we go back to Turner's op-ed in Bloomberg from this morning in which he says:

> ***Many people are legitimately angry that few bankers have been punished****. Some were incompetent, others dishonest. Yet they were not a fundamental driver of the crisis any more than the misbehavior of individual financiers in 1920s America caused the Great Depression.*

The hypocrisy is astounding: in one paper Turner promotes a policy that will perpetuate, and reward, the banking status quo, and in another letter he urges punishment for the very same bankers who will benefit the most from having robbed the middle class for the past 7 years***thanks to policies enacted by people like him***!

The sad truth, however, is that after reading the above, one barely even has the energy to feel disgust.

But perhaps just to help spark if not disgust then a little bit of anger, we will conclude with the quote used by Turner at the very top of his paper which confirms that at least one person knew how it was all going to end a long time ago:

> ***"Consider for example a tax cut for households and businesses that is explicitly coupled with incremental Bank of Japan purchases of government debt – so that the tax cut is in effect financed by money creation"***

Ben Bernanke, *Some Thoughts on Monetary Policy in Japan, 2003*

* * *

Source: The Case for Monetary Finance – An Essentially Political Issue.

- Here Come The Money Helicopters!

Abe's economics textbook – it's not working, so maybe they should do more of it?

Cartoon by Li Feng

And now cometh Etsuro Honda, a special advisor to Mr. Abe and often described as an "architect" of Abenomics. Mr. Honda says it may be premature to say Japan is in recession. Instead, he describes the economy as "static."

In yesterday's interview with the Financial Times, **Honda took no blame for the slowdown, even though he, as much as any living human being, is clearly responsible for it. Instead, he proposes to go "full retard," with even more imbecilic policies.**

Japan has a nigh endless supply of insane Keynesians doing the same thing over and over and over again – here is one more, Etsuro Honda. His proposal? Let's go full retard. Doesn't he know that no matter what you do, you should *never* go full retard?

QE for the People

This, we fear, is not just a freaky sideshow. It is more like the coming attractions. Japan has led the world for the last three decades – first with an unsustainable bubble economy in the 1980s… then with a meltdown… followed by a long on-again-off-again recession.

The Japanese feds tried every trick in the book to revive the economy – except for the one that would have worked. The government borrowed and spent (as a percentage of the economy) more than any nation had ever done. And it invented ZIRP and QE as policy tools.

But now it's become "urgent," says Honda, to do more. Hasn't he done enough already? you may ask. But no… He now proposes more QQE (for "qualitative and quantitative easing"). What grotesquerie lies ahead?

Our mouth hangs open. What is this strange beast slouching towards the Eccles Building (the headquarters of the U.S. Fed)…waiting to be born? **The idea behind Japan's quantitative easing was to INCREASE the quantity of money in the system so as to DECREASE the quality of each unit.**

It was expressly meant to devalue the yen so that consumers would want to get rid of their currency faster. QQE makes no sense… even in the perverse terms of modern central bank meddling.

Here is how the money will come back from its hideout in money heaven – via helicopter! Look how happy the peasants are!

Illustration via adamsmith.org

But wait. There's more. Honda says it will be accompanied by a "supplementary budget, focusing on the real income shortage of mid- and low-income households."

Right now, this proposed extra spending is being funded out of taxes. But **support is growing around the world for such spending to be funded by "People's QE."** The idea behind

"People's QE" is that central banks would directly fund government spending… and even inject money directly into household bank accounts, if need be. And the idea is catching on.

Already the European Central Bank is buying bonds of the European Investment Bank, an E.U. institution that finances infrastructure projects. And the new leader of Britain's Labor Party, Jeremy Corbyn, is backing a British version of this scheme.

Ah-ha! That's the monster coming to towns and villages near you! Call it "overt monetary financing." Call it "money from helicopters." Call in "insane." **But it won't be unpopular.** Who will protest when the feds begin handing our money to "mid- and low-income households"?

We wait. We watch. We wonder how the Japanese will attempt to bring back to life the economy they have worked so hard to kill. And now, all over the world, central planners, bankers, and politicians are watching too. "Where goest the Bank of Japan, there too I shall go," they tell themselves.

- The Next Thing Might Be Helicopter Money James Grant (Interest rate Observer)

What's new and different (*since 2007*) is the larger than life presence of government in our markets, both with respect to regulation and with respect to the management and the production and the manipulation of money.

We are living in the age of magical thinking.

Governments through central banks have muscled down money market interest rates to zero and in some cases below zero. Not content with that, they have implemented what economists chose to call «the portfolio balance channel». That's a very fancy phrase meaning higher stock prices in the interest of rising aggregate demand.

This is a monetary moment. I think we are looking at the beginning of the world's reappraisal of the words and deeds of central bankers like Janet Yellen and Mario Draghi. What we're waiting for is a sufficient recognition of the monetary disorder. You see monetary disorder manifested in super low interest rates, in the mispricing of credit broadly and you see it in the escalation of radical monetary nastrums that are floating out of the various central banks and established temples of thought:

Negative real rates,

Negative nominal rates and

The idea of helicopter money.

So you need some hedge against things.

The global financial markets are under severe stress. The postponed interest rate hike in the United States, the fast cool down of the Chinese economy and the crash in the commodity complex are causing a great amount of unease among investors. Fear is growing that the world slips into recession.

What do you think this will look like?
They (*central bankers*) don't keep those things (*new policy initiatives*) as a secret. ***They talk quite openly about «direct monetary funding» which is what Milton Friedman had in mind when he coined the phrase "helicopter money". So the next idea is just bypassing the banking system altogether and mailing out checks to the citizens.***

Would something like that even work?
All this monetary stimulus does two things in a reciprocal way: It pushes failure into the future and brings consumption into the present. Providing marginal businesses with very cheap credit is inviting companies that have passed their useful days of their commercial lives to pretending some kind of an afterlife thanks to the subsidies from the central banks. But capitalism is inherently a dynamic system based on entrepreneurship and to new inventions. It's a little bit like the forest for the trees: You need life but you also need death. Without death there is no room for a new generation and what you get is Japan: Standing timbers of ancient age, none of them too healthy. Quantitative easing and artificially low interest rates reduce the dynamics, the growth and the vibrancy of economic life.

- Time for the Nuclear Option Raining Money on Main Street

Virtually all money today is created as bank debt, but people can no longer take on more debt.

Predictions are that we will soon be seeing the "nuclear option" - central bank-created money injected directly into the real economy. All other options having failed, governments will be reduced to issuing money outright to cover budget deficits. So warns a September 18 article on ZeroHedge titled "It Begins: Australia's Largest Investment Bank Just Said 'Helicopter Money' Is 12-18 Months Away."

Money reformers will say it's about time. Virtually all money today is created as bank debt, but people can no longer take on more debt. The money supply has shrunk along with people's ability to borrow new money into existence. Quantitative easing (QE) attempts to re-inflate the money supply by giving money to banks to create more debt, but that policy has failed. It's time to try dropping some debt-free money on Main Street.

The Zerohedge prediction is based on a release from Macqurie, Australia's largest investment bank. It notes that GDP is contracting, deflationary pressures are accelerating, public and private sectors are not driving the velocity of money higher, and central bank injections of liquidity are losing their effectiveness. Current policies are not working. As a result:

There are several policies that could be and probably would be considered over the next 12-18 months. If private sector lacks confidence and visibility to raise velocity of money, then (arguably) public sector could. In other words, instead of acting via bond markets and banking sector, *why shouldn't public sector bypass markets altogether and inject stimulus directly into the 'blood stream'*? Whilst it might or might not be called QE, it would have a much stronger impact and unlike the last seven years**,** the recovery could actually mimic a conventional business cycle and investors would soon start discussing multiplier effects and positioning in areas of greatest investment**.**

Willem Buiter, chief global economist at Citigroup, is also recommending "helicopter money drops" to avoid an imminent global recession, stating:

A global recession starting in 2016 led by China is now our Global Economics team's main scenario. Uncertainty remains, but the likelihood of a timely and effective policy response seems to be diminishing. . . .

Helicopter money drops in China, the euro area, the UK, and the U.S. and debt restructuring . . . can mitigate and, if implemented immediately, prevent a recession during the next two years without raising the risk of a deeper and longer recession later.

Corbyn's PQE

In the UK, something akin to a helicopter money drop was just put on the table by Jeremy Corbyn, the newly-elected Labor leader. He proposes to give the Bank of England a new mandate to upgrade the economy to invest in new large scale housing, energy, transport and digital projects. He calls it "quantitative easing for people instead of banks" (PQE). The investments would be made through a National Investment Bank set up to invest in new infrastructure and in the hi-tech innovative industries of the future.

Australian blogger Prof. Bill Mitchell agrees that PQE is economically sound. But he says it should not be called "quantitative easing." QE is just an asset swap - cash for federal securities or mortgage-backed securities on bank balance sheets. What Corbyn is proposing is actually Overt Money Financing (OMF) - injecting money directly into the economy.

Mitchell acknowledges that OMF is a taboo concept in mainstream economics. Allegedly, this is because it would lead to hyperinflation. But the real reasons, he says, are that:

1. It cuts out the private sector bond traders from their dose of corporate welfare which unlike other forms of welfare like sickness and unemployment benefits etc. has made the recipients rich in the extreme. . . .
2. It takes away the 'debt monkey' that is used to clobber governments that seek to run larger fiscal deficits.

OMF as a Solution to the EU Crisis

Mitchell observes that OMF has actually been put on the table by the European Parliament. According to a Draft Report by the Committee on Economic and Monetary Affairs on the European Central Bank Annual report for 2012, the European Parliament:

9. Considers that the monetary policy tools that the ECB has used since the beginning of the crisis, while providing a welcome relief in distressed financial markets, have revealed their limits as regards stimulating growth and improving the situation on the labour market; considers, therefore, that the ECB could investigate the possibilities of implementing new unconventional measures aimed at participating in a large, EU-wide pro-growth programme, including the use of the Emergency Liquidity Assistance facility to undertake an 'overt money financing' of government debt in order to finance tax cuts targeted on low-income households and/or new spending programmes focused on the Europe 2020 objectives;
10. Considers it necessary to review the Treaties and the ECB's statutes in order to establish price stability together with full employment as the two objectives, on an equal footing, of monetary policy in the eurozone;

These provisions were amended out of the report, says Prof. Mitchell, largely due to German hyperinflation paranoia. But he maintains that Overt Money Financing is the most effective way to solve the Eurozone crisis without tearing down the monetary union:

1. It amounts to the ECB telling member states that they will provide the Euros to permit sufficient deficit spending aimed at increasing employment and production.
2. No public debt is issued.
3. No taxes are raised.
4. Interest rates would not rise.
5. A Job Guarantee could be introduced immediately.
6. The Troika can retire - no more bailouts.
7. As growth returns, structural changes - better public services, better schools, better health care etc. can be implemented. Growth allows structural changes to occur more quickly because people are happy to move between jobs if there are jobs to move between.

The Bogus Inflation Objection

Tim Worstall, writing in the UK Register, objects to Corbyn's PQE (or OMF) on the ground that it cannot be "sterilized" the way QE can. When inflation hits, the process cannot be reversed. If the money is spent on infrastructure, it will be out there circulating in the economy and will not be retrievable. Worstall writes:

QE is designed to be temporary, . . . because once people's spending rates recover we need a way of taking all that extra money out of the economy. So we do it by using printed money to buy bonds, which injects the money into the economy, and then sell those bonds back once we need to withdraw the money from the economy, and simply destroy the money we've raised. . . .

If we don't have any bonds to sell, it's not clear how we can reduce [the money supply] if large-scale inflation hits.

The problem today, however, is not inflation but deflation of the money supply. Some consumer prices may be up, but this can happen although the money supply is shrinking. Food prices, for example, are up; but it's because of increased costs, including drought in California, climate change, and mergers and acquisitions by big corporations that eliminate competition.

Adding money to the economy will not drive up prices until demand is saturated and production has hit full capacity; and we're a long way from full capacity now. Before that, increasing "demand" will increase "supply." Producers will create more goods and services. Supply and demand will rise together and prices will remain stable. In the US, the output gap - the difference between actual output and potential output - is estimated at about $1 trillion annually. That means the money supply could be increased by at least $1 trillion annually without driving up prices.

Don't Sterilize - Tax!

If PQE does go beyond full productive capacity, the government does not need to rely on the central bank to pull the money back. It can do this with taxes. Just as loans increase the money supply and repaying them shrinks it again, so taxes and other payments to the government will shrink a money supply augmented with money issued by the government.

Using 2012 figures (drawing from an earlier article by this author), the velocity of M1 (the coins, dollar bills and demand deposits spent by ordinary consumers) was then 7. That means M1 changed hands seven times during 2012 - from housewife to grocer to farmer, etc. Since each recipient owed taxes on this money, increasing M1 by one dollar increased the tax base by seven dollars.

Total tax revenue as a percentage of GDP in 2012 was 24.3%. Extrapolating from those figures, $1.00 changing hands seven times could increase tax revenue by $7.00 x 24.3% = $1.70. That means the government could, in theory, get more back in taxes than it paid out. Even with some leakage in those figures and deductions for costs, all or most of the new money spent into the economy might be taxed back to the government. New money could be pumped out every year and the money supply would increase little if at all.

Besides taxes, other ways to get money back into the Treasury include closing tax loopholes, taxing the $21 trillion or more hidden in offshore tax havens, and setting up a system of public banks that would return the interest on loans to the government. Net interest collected by U.S. banks in 2014 was $423 billion. At its high in 2007, it was $725 billion.

Thus there are many ways to recycle an issue of new money back to the government. The same money could be spent and collected back year after year, without creating price inflation or hyperinflating the money supply.

This not only could be done; it needs to be done. Conventional monetary policy has failed. Central banks have exhausted their existing toolboxes and need to explore some innovative alternatives.

- Where Is the First Helicopter Drop of Money Likely to Land
- The Endgame Takes Shape- -Banning Capitalism And Bypassing Capital Markets

NIRP – *Negative Interest Rate Policy*

NIRP – *Negative Interest Rate Policy*

Negative Interest Rates the New Normal Next Time Economies Slump

Deutsche Bank suggests ECB may never lift deposit rate above 0

Now that Sweden and Switzerland have shown that negative benchmark interest rates don't necessarily result in flights to cash, asset bubbles or banking strains, the global giants of central banking may be more willing to embrace sub-zero borrowing costs the next time their economies slide.

"There's a very real chance unorthodoxy becomes the new orthodoxy," said Alan Ruskin, global head of Group-of-10 currency strategy at Deutsche Bank AG in New York.

While financial markets are focused on the Federal Reserve's looming rate increase, policy makers and economists are already changing their attitude toward negative rates.

European Central Bank President Mario Draghi is open to reducing the rate he charges banks to leave money in his coffers overnight further into negative territory. Bank of England Governor Mark Carney has also revised his thinking to say the U.K. benchmark could fall below 0.5 percent if needed having previously worried deeper cuts would roil money markets.

Meantime, Fed Chair Janet Yellen said last week that "if circumstances were to change" then "potentially anything, including negative interest rates, would be on the table." One of her policy-setting colleagues has already advocated them for next year.

Plumbing new depths the next time economies stumble would continue the pattern of the past few decades in which each of the peaks and troughs in rates were more often than not lower than in the previous business cycle.

Back in 1984, Fed Chair Paul Volcker lifted the federal funds rate to 11.75 percent before cutting it to 5.88 percent two years later. By contrast, the last expansion saw the benchmark top out at just 5.75 percent before being cut to near zero.

The Federal Reserve's Benchmark Rate Since 1980

Reasons for the pattern include the success in squeezing inflation out of economies that had been plagued by double-digit price gains in the early 1980s. The decline in volatility gave officials more room to try to stoke demand and, critics would say, asset bubbles.

A glut of savings also played a part. along with the the argument that the natural rate of interest, the level at which inflation is stable and output at trend, has been in decline for decades.

The aim of negative rates is to spur spending and lending by penalizing savers and banks sitting on cash. It also helps that they tend to weaken currencies.

Sweden's key rate is already minus 0.35 percent and Switzerland's is minus 0.75 percent. The ECB's deposit rate is minus 0.2 percent and may be cut further next month, while Denmark's is minus 0.75 percent.

Lower Peaks

Central bankers are already signaling when they do lift rates they will do so by less than last time, preserving the trend of lower peaks. The median estimate of Fed policy makers is for the long-run neutral fed funds rate to be 3.5 percent. Carney talks of raising rates in a "limited and gradual" way.

Richard Barwell, an economist at BNP Paribas Asset Management, argues that policy makers will still hope to use regulatory tools more next time their economies are in trouble, reducing the need for monetary stimulus. It's also premature to say that rates will be lower than in the past, he said.

Ruskin nevertheless holds out the possibility that leading central banks will go negative next time and even that the ECB's deposit rate may not see positive territory again.

"It's not even clear you're going to get zero at the peak of the cycle in Europe," he said. "One hopes U.S. rates will be meaningfully positive in the next cycle, but that can't be taken for granted in Europe."

- Yellen Tells Congress Negative Interest Rates Are Possible
- Yellen on Negative Interest Rates
- The Fed is Already -Testing the Waters- For NIRP
- Fed officials seem ready to deploy negative rates in next crisis
- Federal Reserve Calling For A Negative Interest Rate Policy

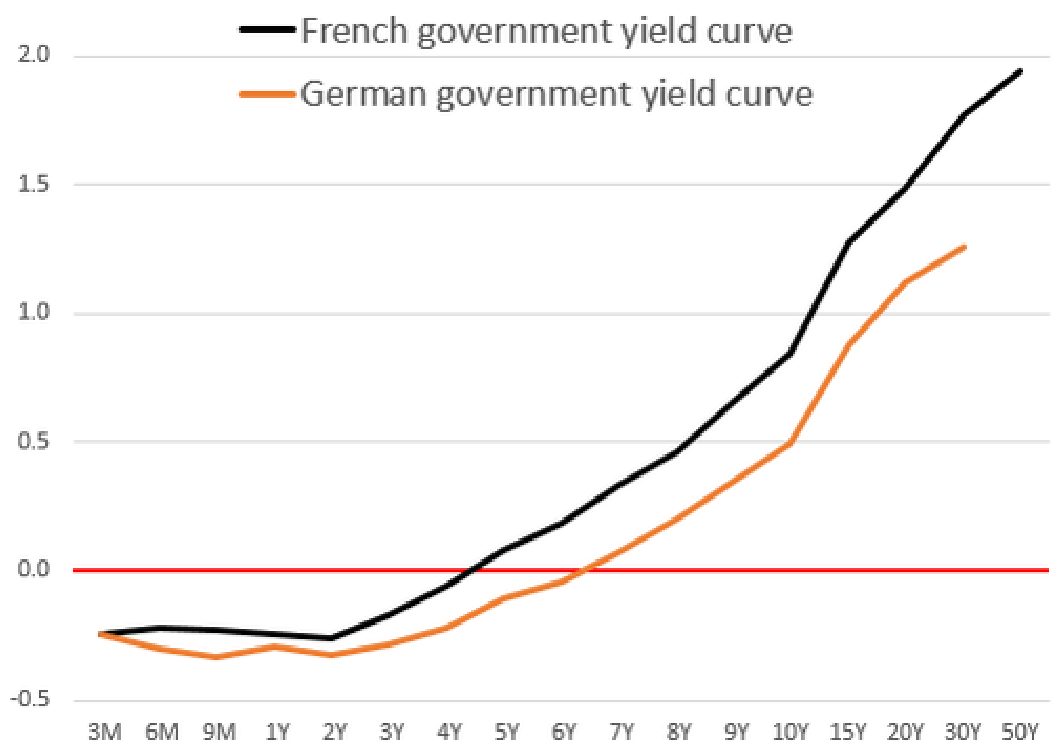
- Santelli & Hunt Warn About -Dire Consequences- Of Negative Rates
- How Sweden's negative interest rates experiment turned economics on its head
- NIRP Goes To Nippon- Japan Auctions 1 Year Paper At Most Negative Yield On Record

- Talk of Negative Interest Rates Point to Increasingly Desperate Situation
- The Mindless Stupidity Of Negative Interest Rates
- Banks Turn Down Deposits As Stealth NIRP Takes Hold
- Fed Experts Call for NIRP… is a Physical Cash Ban Next
- NIRP, its likelihood and effect on commodities

Yield continues to schatz itself... GERMAN TWO-YEAR NOTE YIELD DROPS TO RECORD-LOW MINUS 0.35%

Italian 2-year yields turns negative for the first time in history

France and Germany's yield curves are negative out to 4Y and 6Y, respectively



WAR ON CASH – *The Impediment MUST Be Removed*

Just a few selected research pieces of the Stealth War on Cash going on:

- Why The Powers That Be Are Pushing A Cashless Society

We Can't Rein In the Banks If We Can't Pull Our Money Out of Them

Martin Armstrong summarizes the headway being made to ban cash, and argues that the goal of those pushing a cashless society is to prevent bank runs ... and increase their control:

The central banks are ... planning drastic restrictions on cash itself. They see moving to electronic money will first eliminate the underground economy, but secondly, they believe it will even prevent a banking crisis.This idea of eliminating cash was first floated as the normal trial balloon to see how the people take it. It was first launched by Kenneth Rogoff of Harvard University and Willem Buiter, the chief economist at Citigroup. Their claims have been widely hailed and their papers are now the foundation for the new age of Economic Totalitarianism that confronts us. Rogoff and Buiter have laid the ground work for the end of much of our freedom and will one day will be considered the new Marx with hindsight. They sit in their lofty offices but do not have real world practical experience beyond theory. Considerations of their arguments have shown how governments can seize all economic power are destroy cash in the process eliminating all rights. Physical paper money provides the check against negative interest rates for if they become too great, people will simply withdraw their funds and hoard cash. Furthermore, paper currency allows for bank runs. Eliminate paper currency and what you end up with is the elimination of the ability to demand to withdraw funds from a bank.

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In many nations, specific measures have already been taken demonstrating that the Rogoff-Buiter world of Economic Totalitarianism is indeed upon us. This is the death of Capitalism. Of course the socialists hate Capitalism and see other people's money should be theirs. What they cannot see is that Capitalism is freedom from government totalitarianism. The freedom to pursue the field you desire without filling the state needs that supersede your own.

There have been test runs of this Rogoff-Buiter Economic Totalitarianism to see if the idea works. I reported on June 21, 2014 that Britain was doing a test run. A shopping street in Manchester banned cash as part of an experiment to see if Brits would accept a cashless society. London buses ended accepting cash payments from July 2014. Meanwhile, Currency Exchange dealers began offering debt cards instead of cash that they market as being safer to travel with. The Chorlton, South Manchester experiment was touted to test customers and business reaction to the idea for physical currency will disappear inside 20 years.

France passed another Draconian new law that from the police parissummer of 2015 it will now impose cash requirements dramatically trying to eliminate cash by force. French citizens and tourists will then only be allowed a limited amount of physical money. They have financial police searching people on trains just passing through France to see if they are transporting cash, which they will now seize. Meanwhile, the new French Elite are moving in this very same direction. Piketty wants to just take everyone's money who has more than he does. Nobody stands on the side of freedom or on restraining the corruption within government. The problem always turns against the people for we are the cause of the fiscal mismanagement of government that never has enough for themselves.

In Greece a drastic reduction in cash is also being discussed in light of the economic crisis. Now any bill over €70 should be payable only by check or credit card – it will be illegal to pay in cash. The German Baader Bank founded in Munich expects formally to abolish the cash to enforce negative interest rates on accounts that is really taxation on whatever money you still have left after taxes.

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Complete abolition of cash threatens our very freedom and rights of citizens in so many areas.

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Paper currency is indeed the check against negative interest rates. We need only look to Switzerland to prove that theory. Any attempt to impose say a 5% negative interest rates (tax) would lead to an unimaginably massive flight into cash. This was already demonstrated recently by the example of Swiss pension funds, which withdrew their money from the bank in a big way and now store it in vaults in cash *in order to escape the financial repression. People will act in their own self-interest and negative interest rates are likely to reduce the sales of government bonds and set off a bank run as long as paper money exists.*

Obviously, government and bankers are not stupid. The only way to prevent such a global bank run would be the total prohibition of paper money. This is unlikely, both in Switzerland and in the United States because the economies are dominated there by a certain "liberalism" to some extent but also because their currencies also circulate outside their domestic economies. The fact that but the question of the cash ban in the context of a global conference with the participation of the major central banks of the US and the ECB will be discussed, demonstrates by itself that the problem is not a regional problem.

Nevertheless, there is a growing assumption that the negative interest rate world (tax on cash) is likely to increase dramatically in Europe in particular since it is socialism that is collapsing. Government in Brussels is unlikely to yield power and their line of thinking cannot lead to any solution. The negative interest rate concept is making its way into the United States at J.P. Morgan where they will charge a fee on excess cash on deposit starting May 1st, 2015. Asset holdings of cash with a tax or a fee in the amount of the negative interest rate seems to be underway even in Switzerland.

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The movement toward electronic money is moving at high speed and this says a lot about the state of the financial system. The track record of the major financial institutions is nearly perfect – they are always caught on the wrong side when a crisis breaks, which requires their bailouts. The fact that we have already seen test runs with theory-balloons flying, the major financial institutions are in no shape to withstand another economic decline.

For depositors, this means they really need to grasp what is going on here for unless they are vigilant, there is a serious risk of losing everything. We must understand that these measures will be implemented overnight in the middle of a banking crisis after 2015.75. The balloons have taken off and the discussions are underway. The trend in taxation and reduction of cash seems to be unstoppable. Government is not prepared to reform for that would require a new way of thinking and a loss of power. That is not a consideration. They only see one direction and that is to take us into the new promised-land of economic totalitarianism.

People can't pull cash out of their bank accounts – for political reasons, because they've lost confidence in the bank, or because "bail-ins" are enacted – if cash is banned.

The Financial Times argued last year that central banks would be the real winners from a cashless society:

Central bankers, after all, have had an explicit interest in introducing e-money from the moment the global financial crisis began…

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The introduction of a cashless society empowers central banks greatly*. A cashless society, after all,* ***not only makes things like negative interest rates possible,*** *it* ***transfers absolute control of the money supply to the central bank****, mostly by turning it into a universal banker that competes directly with private banks for public deposits. All digital deposits become base money.*

The Government Can Manipulate Digital Accounts More Easily than Cash

Moreover, an official White House panel on spying has implied that the government is manipulating the amount in people's financial accounts.

If all money becomes digital, it would be much easier for the government to manipulate our accounts.

Indeed, numerous high-level NSA whistleblowers say that NSA spying is about crushing dissent and blackmailing opponents … not stoppingterrorism.

This may sound over-the-top … but remember, the government sometimes labels its critics as "terrorists". If the government claims the power to indefinitely detain – or even assassinate – American citizens at the whim of the executive, don't you think that government people would be willing to shut down, or withdraw a stiff "penalty" from a dissenter's bank account?

If society becomes cashless, dissenters can't hide cash. All of their financial holdings would be vulnerable to an attack by the government.

This would be the ultimate form of control. Because – without access to money – people couldn't resist, couldn't hide and couldn't escape.

- Bank Of Ireland Bans -Small- Cash Withdrawals At Branches
- Bundesbank Chief Says -Nein- To Cash Ban
- Is a Ban on Physical Cash Coming Soon
- More and More Countries Join the War on Cash

More and More Countries Are Beginning to Outlaw Cash for Certain Transactions 10-24-15 Graham Summers

More and more institutions are trying to make it harder for you to move your money into cash.

Globally, over $5 trillion in debt currently have negative yields in **nominal terms**, meaning the bond literally has a negative yield when it trades. In the simplest of terms this means that investors are PAYING to own these bonds.

Bonds are not unique in this regard. Switzerland, Denmark and other countries are now charging deposits at their banks. France and Italy have banned any transaction over €1,000 Euros from using physical cash. Spain has already banned transactions over €2,500. Uruguay has banned transactions over $5,000. And on and on.

This is also at work in the US. Louisiana has made it illegal to purchase second hand goods using cash. This is just the beginning. The War on Cash will be spreading in the coming weeks.

The reasoning is simple. Most large financial entities are insolvent. As a result, if a significant amount of digital money is converted into actual physical cash, the firm would very quickly implode.

This is true for banks around the world. European banks as a whole are leveraged at 26 to 1. In simple terms, this means they have just €1 in capital for every €26 in assets (bought via borrowed money). If a significant percentage of their depositors took their money out of the bank, the bank would violate its capital limitations at best and implode at worse.

The US financial system isn't any better. Indeed, the vast majority of it is in digital money. Actual currency is just a little over $1.36 trillion. Bank accounts are $10 trillion. Stocks are $20 trillion and Bonds are $38 trillion.

And at the top of the heap are the derivatives markets, which are over $220 TRILLION.

Notice that less than 1% of the "wealth" in this system is actual physical cash. Now imagine what would happen if investors decided to move their money out of the system and into physical cash.

This is precisely what imploded the money market system during the 2008 crisis.

If you think the banks aren't terrified of what this market could do to them, consider that JP Morgan managed to get Congress to put the US taxpayer on the hook for it derivatives trades. **Mind you, this is the same bank that is now refusing to let clients store cash in safe deposit boxes.**

This is just the beginning. As anyone can tell you, it's all but impossible to move large amounts of money into cash in the US. Even the large banks will routinely ask you for 24 hours notice if you need $10,000 or more in cash. These are banks will TRLLLIONS of dollars worth of assets on their books.

This is just the beginning.

- Physical Cash Poses a HUGE Problem For Central Banks
- Why Government Hates Cash

- Why the Fed HATES Physical Cash and Could Move to Tax It
- The World's First Cashless Society Is Here - A Totalitarian's Dream Come True

My Macro Analytics guest *Nick Giambruno of InternationalMan.com,* recently wrote this research piece:

Central planners around the world are waging a War on Cash. In just the last few years:

- Italy made cash transactions over €1,000 illegal;
- Switzerland proposed banning cash payments in excess of 100,000 francs;
- Russia banned cash transactions over $10,000;
- Spain banned cash transactions over €2,500;
- Mexico made cash payments of more than 200,000 pesos illegal;
- Uruguay banned cash transactions over $5,000; and
- France made cash transactions over €1,000 illegal, down from the previous limit of €3,000.

The War on Cash is a favorite pet project of the economic central planners. They want to eliminate hand-to-hand currency so that governments can document, control, and tax everything.

This is why they're lowering the threshold for mandatory reporting of cash transactions and, in some instances, simply making it illegal to pay cash.

In the U.S., central planners ratchet up the War on Cash every time the government declares a made-up war on something else…a war on crime, a war on drugs, a war on poverty, a war on terror…

They all end with more government intrusion into your financial affairs.

Thanks to these made-up wars, the U.S. government is imposing an increasing number of regulations on cash transactions. Try withdrawing more than $10,000 in cash from your bank. They'll treat you like a criminal or terrorist.

The Federal Reserve is at the center of the War on Cash. Its weapons are inflation and control over the currency denominations.

Take the $100 note, for example. It's the largest bill in circulation today. This was not always the case. At one point, the U.S. had $500, $1,000, $5,000, and even $10,000 notes. But the government eliminated these large notes in 1969 under the pretext of fighting the War on Some Drugs.

Since then, the $100 note has been the largest. But it has far less purchasing power than it did in 1969. Decades of rampant money printing have inflated the dollar. Today, a $100 note buys less than a $20 note did in 1969.

Even though the Federal Reserve has devalued the dollar over 80% since 1969, it still refuses to issue notes larger than $100. This makes it inconvenient to use cash for large transactions, which forces people to use electronic payment methods.

This, of course, is what the U.S. government wants.

It's exactly like Ron Paul said: ***"The cashless society is the IRS's dream: total knowledge of, and control over, the finances of every single American."***

Policymakers or Central Planners?

On stories related to the War on Cash, you may have noticed that the mainstream media often uses the word "policymakers," as in "policymakers have decided to keep interest rates at record low levels."

When the media uses "policymakers," they are often referring to central bank officials. It's a curious word choice. As far as I can tell, there is no difference between a policymaker and central planner.

Most people who want to live in a free society agree that central planning is not a good idea. So the media uses a different word to put a more neutral spin on things.

To help you think more clearly, I suggest substituting "central planners" every time you see "policymakers."

<u>The World's First Cashless Society</u>

In 1661, Sweden became the first country in Europe to issue paper money. Now it's probably going to be the first in the world to eliminate it.

Sweden has already phased out most cash transactions. According to Credit Suisse, **80% of all purchases in Sweden are electronic and don't involve cash. And that figure is rising.**

If the trend continues - and there is nothing to suggest it won't - Sweden could soon be the world's first cashless society.

Sweden's supply of physical currency has dropped over 50% in the last six years. A couple of major Swedish banks no longer carry cash. Virtually all Swedes pay for candy bars and coffee electronically. Even homeless street vendors use mobile card readers.

Plus, an increasing number of government restrictions are encouraging Swedes to dump cash. The pretexts are familiar…fighting terrorism, money laundering, etc. In effect, these restrictions make it inconvenient to use cash, so people don't.

<u>So far, Swedes have passively accepted the government and banks' drive to eliminate cash. The push to destroy their financial privacy doesn't seem to bother them. This is likely because the average Swede places an unreasonable amount of trust in government and financial institutions.</u>

<u>Their trust is certainly misplaced.</u> On top of the obvious privacy concerns, eliminating cash enables the central planners' latest gimmick to goose the economy: Negative interest rates.

<u>Making The Negative Interest Rate Scam Possible</u>

Sweden, Denmark, and Switzerland all have negative interest rates.

Negative interest rates mean the lender literally pays the borrower for the privilege of lending him money. It's a bizarre, upside down concept.

But negative rates are not some European anomaly. The Federal Reserve discussed the possibility of using negative interest rates in the U.S. at its last meeting.

Negative rates could not exist in a free market. They destroy the impetus to save and build capital, which is the basis of prosperity.

When you deposit money in a bank, you are lending money to the bank. However, with negative rates you don't earn interest. Instead, you pay the bank.

If you don't like that plan, you can certainly stash your cash under the mattress. As a practical matter, this limits how far governments and central banks can go with negative interest rates. The more it costs to store money at the bank, the less inclined people are to do it.

Of course, central planners don't want you to withdraw money from the bank. This is a big reason why they want to eliminate cash...so you can't. As long as your money stays in the bank, it's vulnerable to the sting of negative interest rates and also helps to prop up the unsound fractional reserve banking system.

If you can't withdraw your money as cash, you have two choices: You can deal with negative interest rates...or you can spend your money. Ultimately, that's what our Keynesian central planners want. They are using negative interest rates and the War on Cash to force you to spend and "stimulate" the economy.

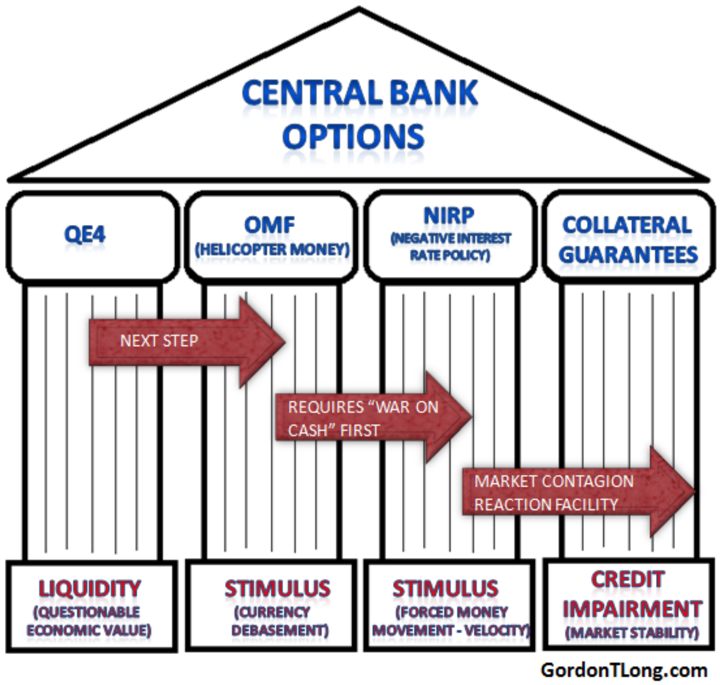
If you ask me, these radical and insane measures are a sign of desperation.

<u>The War on Cash and negative interest rates are huge threats to your financial security. Central planners are playing with fire and inviting a currency catastrophe.</u>

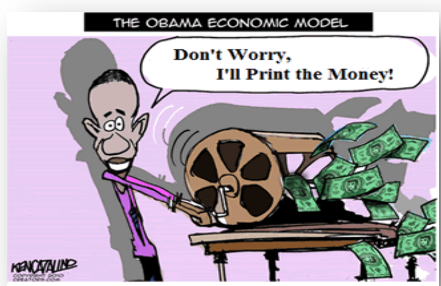
Most people have no idea what really happens when a currency collapses, let alone how to prepare…

COLLATERAL GUARANTEES - *Keeping the Pyramided Debt from Imploding the System*

Because of the degree of rehypothecation (which we written about many times) believe it won't be long before the central bankers are forced to begin guaranteeing a broad array of assets to keep the financial markets from imploding as the previously outlined initiatives all fail.



"Never forget throughout this turmoil: "They will print the money!"



Until No one wants it or Trusts It!

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