Central Banking
East and West since the Crisis

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Remarks at "Changes of Pattern in Global Finance and their Implications"
Shanghai Development Research Foundation (SDRF) /
Friedrich Ebert Stiftung

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Central Banking East and West since the Crisis

I. Measuring Costs of Extraordinary Monetary Policies

- *Three 'Never Befores'*

II. Central Bank Liquidity Provision

- *Regional Variations among the Federal Reserve, European Central Bank, Bank of Japan, People's Bank of China, and Bank of England.*

III. Impact on Financial Markets

- *Review of speculative positions in financial markets … greater market volatility and larger net long positions.*

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Challenges for the Future…

"**Never before**" has there been such:

- Large scale **intervention** by central banks and governments,
- Growth in the financial **regulator apparatus and labyrinth of rules** governing markets,
- **Distortions** across a wide range of financial markets.

"The Unwind: What's Next for Global Markets"
Center for Financial Stability
May 27, 2015

http://www.centerforfinancialstability.org/speeches/unwind_052715.pdf

Major Central Banks: Stock of Liquidity

USD trillion (left axis): 0.0, 1.0, 2.0, 3.0, 4.0, 5.0, 6.0

USD trillion (right axis): 0, 2, 4, 6, 8, 10, 12, 14, 16, 18, 20

2009 2010 2011 2012 2013 2014 2015 2016 2017 2018

BoJ FRB ECB PBoC BoE Total (right axis)

Source: Federal Reserve Board, European Central Bank, Bank of Japan, People's Bank of China, Bank of England, and Center for Financial Stability.

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Major Central Banks: Flow of Liquidity

USD billions

1,600
1,100
600
100
-400
-900

(1)
(2)
(3)

2009
2010
2011
2012
2013
2014
2015
2016
2017
2018

BoJ
FRB
ECB
PBoC
BoE

Source: Federal Reserve Board, European Central Bank, Bank of Japan, People's Bank of China, Bank of England, and Center for Financial Stability.

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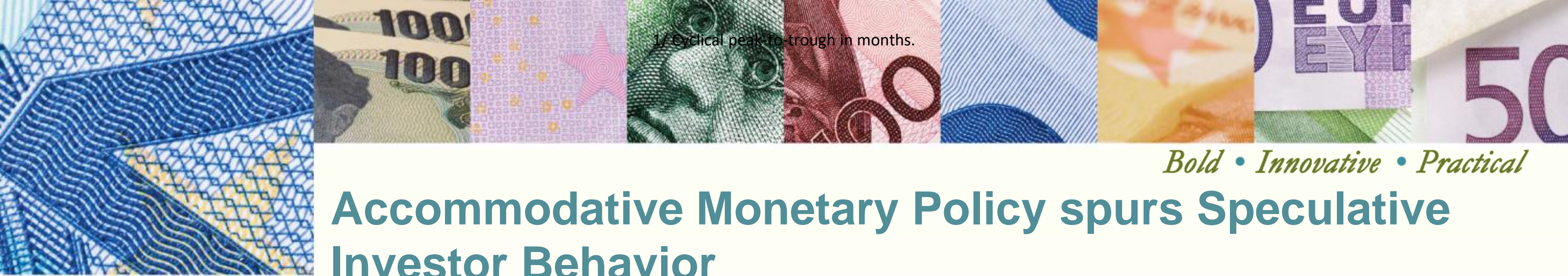


Accommodative Monetary Policy spurs Speculative Investor Behavior

'000 Contracts (Real October 2018 values)

2,000
1,800
1,600
1,400
1,200
1,000
800
600
400
200
0

Jan-93 Jun-95 Nov-97 Apr-00 Sep-02 Feb-05 Jul-07 Dec-09 May-12 Oct-14 Mar-17

Real policy rates fell below 0 in 2002 and remained there until 2006.

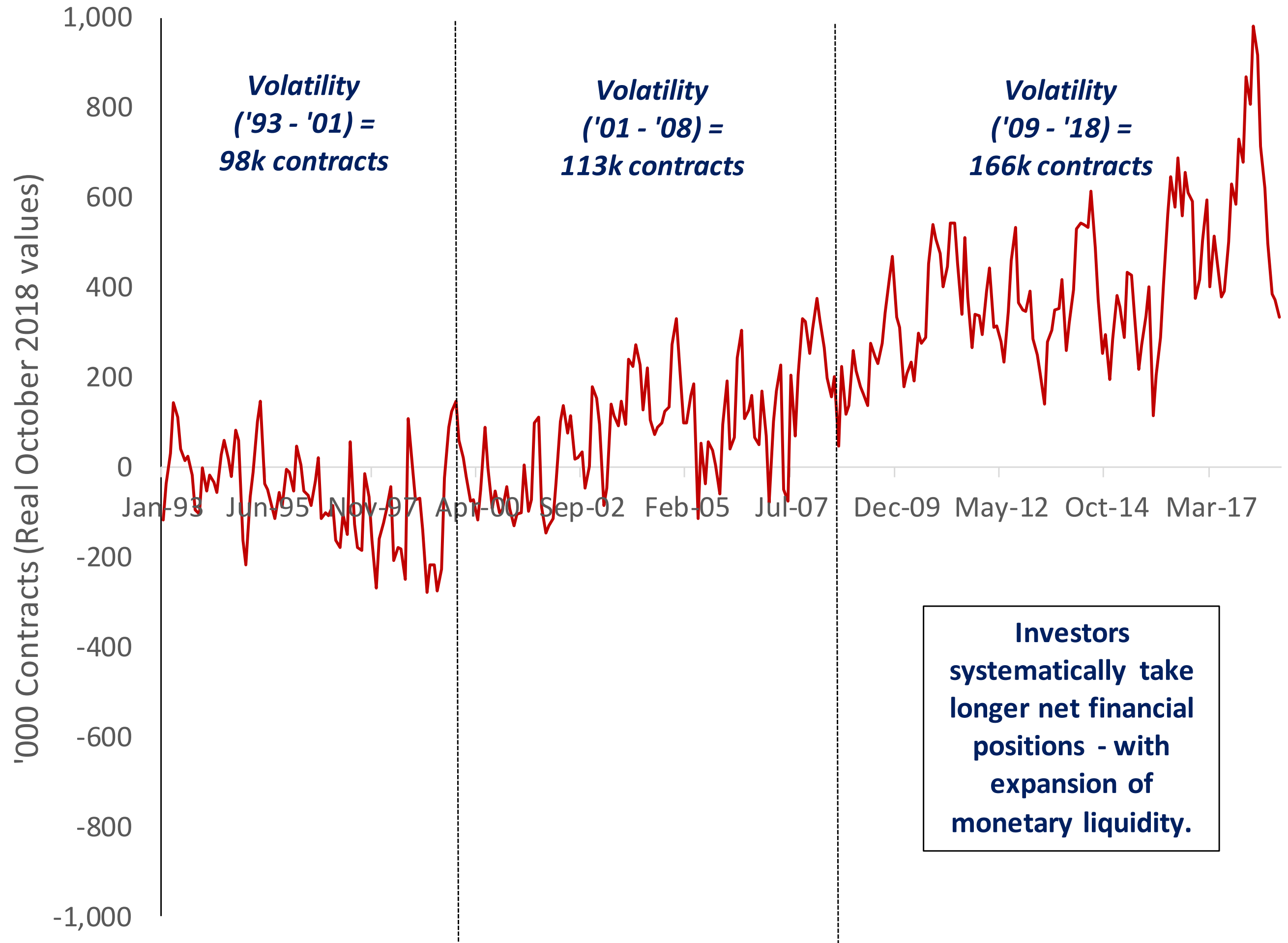
Major Central Bank balance sheets expended from roughly $8 to nearly $18 trillion.

Note: Includes futures positions in NYMEX crude, S&P 500 index, JPY, gold, CHF, Nikkei, and GBP held by speculative investors.
Source: CFTC, Bloomberg LP, and Center for Financial Stability.

1/ Cyclical peak-to-trough in months.

Bold • Innovative • Practical

Accommodative Monetary Policy boosts Volatility and Long Bets



THE WALL STREET JOURNAL.

OPINION

Fixing the Fed's Liquidity Mess

By Lawrence Goodman
And Stephen Dizard

Every Treasury secretary since the late 1930s could proclaim with confidence that the U.S. bond market is the deepest and most liquid in the world. Today's illiquid debt markets threaten the potency of this pledge and put the global economy at risk for another financial crisis.

Fortunately, risks to financial stability radiating from bond markets have captured the attention of the U.S. government. This isn't surprising given the Treasury "flash crash" of Oct. 15, 2014, when a shortage of liquidity hastened a 37 basis-point slide in yields in a mere two hours. Statistically, this equates to a change expected once in over 500 million days.

Quantitative easing and a near-zero interest rate have produced lopsided positions that risk another crisis.

is the backbone for small- and medium-size financial institutions, corporations and credit to individuals.

The Fed should work constructively with private businesses to restore depth and liquidity in major bond markets. And because it will take time to implement solutions, the Fed and other financial regulators should act immediately to do the following:

• Lift the federal-funds rate to neutral levels. The Fed must exit its postcrisis near-zero interest rate policy smoothly and resolutely. The longer it waits the deeper imbalances grow domestically and internationally, as central banks around the world are forced to keep their interest rates well below natural levels.

• Ease restrictions on market finance. Since the 2010 Dodd-Frank law, there has been a collapse in available market liquidity despite more than ample central-bank liquidity. Our data show that the availability of market finance—repurchase agreements, commercial paper and money-market funds—is nearly 30% below a reasonable level to support liquid markets and economic growth.

U.S. financial regulators would be well advised to ease restrictions that

and expertise to the table to organize support for broken markets.

There is substantial private and public capital available to pre-fund liquidity buffers. Cash on corporate balance sheets abounds. The top 100 publicly traded companies in the U.S. hold more than $3.2 trillion in cash and marketable securities. Sovereign-wealth funds, pension funds, insurance companies, private-equity firms and hedge funds also have substantial cash on hand. But the availability of this liquidity does not mean it will be deployed when needed.

Private-sector buffers—developed in concert with the Fed and Treasury—would strengthen the existing legal and market structures and bypass the need for new emergency governmental powers to force capital into markets.

Severe liquidity risks will not heal themselves. To lessen the likelihood of another widespread financial crisis, the time to act is now.

Mr. Goodman is president of the Center for Financial Stability, where Mr. Dizard serves as special counselor.

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Note: Includes futures positions in NYMEX crude, S&P 500 index, JPY, gold, CHF, Nikkei, and GBP held by speculative investors.
Source: CFTC, Bloomberg LP, and Center for Financial Stability.

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