

Quantitative Non-Easing and Weekend Links

Knee-jerk Thoughts on the “Skinny Deal”

- We ended up hitting the (admittedly revised) “base case” I laid out this morning
- I would have preferred the President simply dropped this pretense that we are not decoupling from China, because the ultimate realization will be traumatic for markets. This kabuki theatre act of “decoupling while pretending we’re not” **is not sustainable for the next 13 months.**
- If this ends up being 10-20m tons of bean purchases in exchange for dropping the insignificant October tariffs It’s not a terrible deal for the U.S.
- **The big news today is that the December tariffs were not dropped.** That would have marked a capitulation by Trump.
- **No Huawei dimension** to this trade – Trump retains the chip of offering back access to non-security sensitive products.
- As I wrote this morning, **the currency pact** – “transparency and free market behavior” as I think Mnuchin put it – **is meaningless.**
- **Lighthizer is still hell-bent on enforcement.** As of yet, China has given no indication of flexibility on its “red line” on that issue.
- I don’t see any reason for the next round talks to be more successful than past rounds.
- The politics of capitulation are terrible for Trump
- **This most likely all falls apart between now and December.**
- A possible broader deal could involve a trade of the December tariffs for a substantive deal enforced by a scheduled rollback of the current tariffs, but it’s hard to see China swallowing that.
- Early odds on the Dec tariffs going through: 75%

Quantitative Non-Easing

A few days ago, [when asked by CNBC](#) about the possibility of what DoubleLine Capital's Jeffrey Gundlach had described as "QE lite," Cleveland Fed President Loretta Mester said: "This is nowhere near anything about QE."

Mester is right.

To understand whether or not the Fed's new move to expand the balance sheet by buying short-dated government securities will elicit a change in "monetary policy," we need to drill down into what exactly "money" is. Money is non-interest bearing government debt redeemable on demand "at par."

Various assets have differing degrees of liquidity or "moneyness." By liquidity here we're not talking about "market liquidity" as in bid-offer spreads or market depth. We're talking about monetary liquidity – how easily can you turn the assets into "money."

Compare the benchmark 5-year note with the benchmark 10-year note - both highly "liquid" in terms of availability of prices and market depth.

But they are dissimilar in terms of "moneyness." Both are "redeemable on demand," but not "at par." By dint of its lesser duration, however, the 5-year note is likely to prove less volatile around par than the 10-year note. If your main concern is the ability to turn an asset into "money" on demand, a 5-year note is safer than a ten-year note. It is more "money-like."

Consider a "twist" operation in which the Fed sells more "moneylike" 5-year notes and buys less "moneylike" 10-year notes. Other things equal, this would add "monetary liquidity" to the system. The pool of outstanding assets would be more easily converted into – closer in character to – "money." This increase in systemic "moneyness" - an "easing of liquidity conditions" in the common parlance - connotes an easing of the monetary stance. *Ceteris paribus*, a **"twist" operation is "non-quantitative easing" via the balance sheet.**

Now consider a debt management operation along the lines that [Chairman Powell alluded to the other day](#): a Fed purchase of short-dates Treasuries in exchange for increased issuance of bank reserves.

Bank reserves are no longer technically not "money" by the way. They are redeemable at par, but they pay interest, which is an explicit disincentive to circulation and exchange. With IOER at .25% for most of the post-crisis era, reserves were extremely "money-like." With IOER today at 1.80%, they are considerably less so. Would you call a one-month T-Bill Money? Of course not.



The balance sheet expansion program as described would simply swap one short-dated interest-bearing government liability (reserves) for another (T-bills). The difference in duration (or “moneyness” from this perspective) between these instruments is so negligible as to be meaningless.

The main difference between these two forms of short-dated government debt is that bank reserves count towards the liquidity requirements for Globally Systemically Important Bank, while T-bills don't. That's the point of the exercise – to relieve the pressures those regulations are believed to have put on the repo market via heightened demand for reserves.

If a “twist” operation is “non-quantitative easing,” this recently-touted plan is the opposite: let's call it “Quantitative non-easing.”

As far the outlook for financial markets, there is no need to spend any more time on this issue than this. It is simply not relevant.

On to the links...

The fact that it's been an ugly stretch for U.S.-China relations should not be obscured by an “interim deal” that will amount to little more than a time out.

No more denials – measures to restrict U.S. capital flows to China via multiple channels are in the works. As for the more provocative idea tipped here, it sounds like Pillsbury was asked to inventory the nuclear weapons “just in case.”

[China Trade Talks Restart as White House Explores Escalation Options](#)

Larry Kudlow, the director of the National Economic Council, acknowledged on Tuesday that the administration was looking for ways to protect Americans who were investing in Chinese companies. “We've opened up a study group to take a look at it.”

But the options under consideration go further than that. According to a memo circulated within the White House and reviewed by The New York Times, the administration is studying a menu of actions that, if carried out, would most likely rattle the Chinese government.

*It proposes holding Chinese companies and their employees criminally liable for financial disclosure violations, broadening the criteria that could get prominent Chinese companies blacklisted in the United States and **blocking public and private pension funds and university endowments from certain Chinese investments.***

*Other options go beyond financial scrutiny of Chinese companies. The memo **describes the possibility of fostering deeper ties between the United States and Taiwan** and disrupting the flow of capital between Hong Kong and mainland China if it is determined that Hong Kong's autonomy is not being respected.*

It also lays out legislation in Congress, which Mr. Trump has yet to endorse, that would impose sanctions on China for activity in contested areas of the South China Sea and crack down on Chinese-funded Confucius Institutes at American universities.

Human rights – a new and politically unassailable rationale for decoupling...

[As U.S. Takes Aim at Chinese Tech Firms, Trump Signals a Strategy Shift](#)

In blacklisting surveillance companies, the United States is the first major government to punish China for its crackdown on Muslims.

[Expanded U.S. Trade Blacklist Hits Beijing's Artificial-Intelligence Ambitions](#)

The U.S. decision to add eight Chinese companies to its trade blacklist strikes directly at China's ambitions in artificial intelligence, threatening its companies' access to crucial components and relationships with U.S. firms.

Some of the companies affected are among China's most advanced in core areas of AI, including technology involved in recognizing sounds and faces, autonomous driving and surveillance.

*Although many of the companies targeted have likely been stockpiling components and can shift to backup supply chains, cutting-edge research efforts could slow, given their heavy reliance on advanced U.S. chips. In the long term, **the move could spell an end to partnerships with U.S. companies and institutions** that go back years and limit access to top overseas talent, experts said.*

[People's Daily: Washington blacklisting Chinese entities exposes evil intentions over Xinjiang](#)

Following their recent flagrant interferences in China's Hong Kong, China hawks in Washington are making waves regarding Xinjiang. The U.S. Department of Commerce on Monday added some Chinese entities to its sanctions list. On Tuesday, the U.S. State Department announced visa restrictions on some Chinese officials.



For years, some politicians in Washington have been bent on weaving stories about Xinjiang, while turning a blind eye to the fact that China's policies in the area have achieved remarkable results in maintaining stability and prosperity in that region. Quite different from what these politicians have been peddling around, the most urgent issue in Xinjiang is not about religion or human rights, but rather about combatting extremism and terrorism.

Washington's real motive behind these getting-tough-on-China moves has never been about human rights, but rather about hindering China's development while pretending to claim the high moral ground.

It is high time for those China hawks in Washington to stop interfering in China's domestic issues. And Beijing will take every necessary measure to safeguard its vital interests.

A goodwill gestures ahead of the “interim deal” – the devil will be in the details...

[Trump Green-Lights Some Sales to Huawei](#)

The Trump administration plans to soon issue licenses allowing some American companies to supply non-sensitive goods to the Chinese telecom giant Huawei,

The ban has not technically gone into effect. The administration issued [a temporary reprieve](#) to allow Huawei's suppliers and users of its products more time to find alternate arrangements.

The Trump administration originally said that it would approve licenses to continue selling to Huawei after Mr. Trump met with President Xi Jinping of China in Osaka, Japan, in June. But no licenses have since been issued, raising speculation that the administration was withholding them as leverage in trade talks.

Approving licenses that allow American companies to supply so-called general merchandise to Huawei is likely to be seen as a gesture of good will, though its practical effects may be limited.

[FT: Trump Administration Considers Crackdown on Chinese Contraband](#)

The Trump administration is weighing options to crack down on shipments of contraband goods from China, adding a new point of friction with Beijing.

The White House has been considering an executive order that would increase inspections on parcels from China to detect any illegal contents, according to people familiar with the matter. Administration officials have consulted with big logistics companies as it refines the plan.

“China sends the US close to 1m small air parcels a day, and a disturbingly high per cent appear to contain contraband ranging from counterfeit goods to deadly fentanyl and other opioids,” Peter Navarro, the White House trade and manufacturing policy adviser, said on Wednesday.

China seems keen to release some pressure on the NBA, but I’m not sure this genie can be put back in the bottle on the U.S. side. Multinationals will have increasing difficulty in walking the China P.R. tightrope...

[China Blows Whistle on Nationalistic Protests Against the N.B.A.](#)

After three days of fanning nationalistic outrage, the Chinese government abruptly moved on Thursday to tamp down public anger at the N.B.A. as concerns spread in Beijing that the rhetoric was damaging China’s interests and image around the world.

...a backlash against China could hurt its image in the sporting world ahead of the 2022 Winter Olympics near Beijing. The dispute with the N.B.A. was also quickly politicizing an audience of sports fans who would not normally focus on issues like the protests in Hong Kong.

Editors at state news outlets have told reporters to avoid emphasizing the N.B.A. issue for fear that it might become overheated

[Rubio Urges POTUS to Enforce Anti-Boycott Laws After China's NBA Coercion](#)

U.S. Senator Marco Rubio (R-FL) urged President Donald Trump to fully enforce anti-boycott laws and regulations, and impose penalties against any U.S. persons—including U.S subsidiaries or affiliates of Alibaba Group, JD.com, Tencent, or other Chinese companies—that comply with foreign boycotts intended to bully and coerce American companies or American citizens to conform with the Chinese government and Communist Party’s views, including those related to Hong Kong, Taiwan, Tibet, and other issues.

In the letter Rubio writes, “It is past time that the U.S. take a forceful and unambiguous

stand against the Chinese Government and Communist Party's ongoing efforts to bully and coerce American companies and American citizens to bend to Beijing's will."

[Apple Has Removed A Mapping App That Let Protesters In Hong Kong Track Police](#)

Apple removed from its App Store on Wednesday a popular crowdsourced mapping app called HKmap.live, which let people in Hong Kong track police during the country's ongoing pro-democracy protests.

The removal has sparked outrage from critics who have accused the company of kowtowing to the Chinese government.

Apple removed the app days after the company was criticized in Chinese state media for aiding "rioters" in Hong Kong. An editorial in People's Daily, a government-run newspaper, said: "Letting poisonous software have its ways is a betrayal of Chinese people's feelings."

[China denies manipulating US firms as NBA dispute rumbles on](#)

US Secretary of State Mike Pompeo encouraged more US companies operating in China to challenge Beijing. "I think American businesses are waking up to the risks" inherent in compliance with the Chinese government's rules, he said, according to the transcript of his interview with the PBS NewsHour television program.

[FT: Apple's Diplomatic Dance on China is Coming to an End](#)

Apple's Tim Cook is the corporate world's top diplomat. The 58-year-old chief executive can criticise President Donald Trump's treatment of migrants as "inhumane", denounce his tolerance of white supremacists — and still be invited for cordial talks at the White House.

Overseas, too, Mr Cook's deft political touch is evident. In China, while most of US big tech is barred by Beijing, Mr Cook has turned the country into a \$50bn business for Apple, where a fifth of smartphones are iPhones.

*But now the diplomatic dance is getting more difficult. This is the year when **western business's love affair with social justice messaging has clashed with its growing dependency on China's economy.** It is hard to pretend to be a touchy-feely*

humanitarian company while bowing to a country that imprisons innocent Uighurs on a mass scale.

European Commission's next leaders take tough tone on China

Von der Leyen would be "ready to highlight the differences in equal length with, if not more than, the commonalities shared between the [European Union] and China", an EU source involved in Asian policymaking said.

In real terms, according to multiple sources, Brussels is prepared to build alliances with democratic Asian countries; to speak out more forcefully on China's human rights issues and unfair trade practices; to continue to label China a strategic rival; to encourage more stringent checks on investments from China, especially its state-owned enterprises; and to give Africa and the Balkans a bigger incentive to work with the EU, rather than China.

Hong Kong

The Hong Kong protests might be at a crossroads. While no one wishes for violence, the reality is that peaceful protests are not going to move the CCP. In fact, nothing is going to move the CCP short of domestic upheaval. The only way protestors in Hong Kong can effect that is to entice China to do something that pushes it into international isolation and towards financial crisis. The people of Hong Kong will have to decide how far they want to push things...

Hong Kong Protesters Are Debating a Halt to Vandalism

Hong Kong protesters are debating whether to lower the temperature as the battered financial center girds for another weekend of tear gas and petrol bombs.

Worried that violence and destructive tactics risk alienating more moderate supporters, some activists have urged others to scale back vandalism that has shut shops, banks and train stations across the city. Their concerns include giving Chief Executive Carrie Lam a reason to delay local elections next month or discouraging U.S. lawmakers from passing a bill to support the protest movement.

So far, the movement has enjoyed resilient support in the former British colony as it expanded to include calls for greater democracy. But recent episodes, including protesters ambushing police, throwing Molotov cocktails at officers, beating a taxi



driver and punching a JPMorgan Chase & Co. employee from mainland China have tested the public's tolerance.

However, the view that vandalism should be reduced isn't shared by all. On Thursday, a group of protesters who earlier disrupted transport links to the airport published a plan on LIHKG to pressure commercial establishments Sunday, including a color-coded guide to which establishments should be boycotted or vandalized based on their level of support for the authorities.

This FT piece is ominous and sadly, probably accurate...

[FT, Jamil Anderlini: Beijing Will Have its Revenge on Hong Kong](#)

The calculus of Communist rule does not allow for concessions to unruly provinces. If President Xi Jinping were to compromise and grant Hong Kong the right to vote for its leaders then what about Shanghai or Shenzhen? If he does not harshly punish the territory then the rest of the nation and his many political enemies would smell weakness, rather than applaud his restraint.

Because the people of Hong Kong instinctively understand what is coming, they are unlikely to quietly return to their ordinary lives.

Neither side can back down. So the chances of People's Liberation Army soldiers on the streets of Hong Kong are rising every day as the violence escalates. One senior police official says privately that as many as a quarter of his officers are joining peaceful protests in their spare time. Hated as it is right now, the Hong Kong police force is made up of Cantonese-speaking locals. Faced with a Mandarin-speaking occupying army from the north, many officers would choose to join the rebellion.

This scenario would rob Beijing of the luxury to choose when and how it punishes the city. But vengeance is coming.

The CCP will be immensely unhappy with this dynamic:

[Taiwan's Tsai Ing-wen sends message of defiance to Beijing](#)

Taiwan's president has called on her compatriots to close ranks against China, sounding a message of defiance to Beijing as she gears up to fight for re-election.

“Hong Kong is on the verge of chaos due to the failure of ‘One Country Two Systems’. And still, China is threatening to impose its ‘One Country Two Systems Taiwan model’ on us,” Tsai Ing-wen said on Thursday in a National Day address.

“When freedom and democracy are challenged and the Republic of China’s existence is under threat, we must stand up and defend ourselves,” she added. “As president, standing up to protect national sovereignty is not a provocation — it is my fundamental responsibility.”

China Economy & Markets

I can’t promise I’m not sometimes guilty of over-emphasizing the negative news on these “China Economy and Markets” links, but there really is a dearth of good news out there...

[China Loses a Tech Generation as the Big Payoff Promise Fades](#)

A generation of Chinese tech workers is confronting a new reality as the industry endures its worst slump since the 2008 financial crisis. China’s broader economic slowdown and the trade war with the U.S. have ended the boom that birthed heavyweights including Alibaba Group Holding Ltd. and Tencent Holdings Ltd. Startups in Greater China have raised \$32.5 billion via venture capital deals so far in 2019, less than a third of last year’s \$111.8 billion, data from research and consulting firm Preqin shows. Job losses are mounting, and hiring has slowed: Job postings in the internet and e-commerce sector dropped about 13% in the second quarter, according to recruitment platform Zhaopin. Entrepreneurs are less willing to form ventures, so the pace of startup creation has slowed.

[China’s ‘golden week’ home sales plunge amid property curbs](#)

Property sales in China’s major cities saw one of their worst “golden week” holidays in years, as buyers held back amid a slowing economy and tight restrictions on mortgage loans.

Sales of new homes in Beijing dropped to their lowest level since 2014 during the week following the National Day holiday, according to data from the property information portal Zhuge.com.

By area, sales of new homes in Shanghai plummeted 86 per cent to 5,000 square metres, while the capital saw a 92 per cent plunge to 2,000 sq metre, according to data from Centaline Property.



Traditionally a peak period for sales, the seven-day holiday drew little interest from buyers who were unwilling to pursue big investments at a time when the national economy faces a slowdown caused by the trade war with the United States. Buyers' appetite was further depleted by banks tightening mortgage loans and Beijing's tougher measures to curb home prices.

SCMP: China Slimming Down Belt and Road Initiative

The growth of China's Belt and Road Initiative slowed significantly over the last 18 months as Beijing's overseas lending flattened out and the value of new overseas construction projects declined...

The value of new projects spread across 61 countries involved in the plan fell 13% to US\$126 billion in 2018 compared to the previous year, with the figure falling a further 6.7% in the period up to August 2019. Existing contracts also dropped 4.2% over the first eight months of 2019.

*This is, in part, due to the **level of funds available to invest in other countries having fallen sharply...***

In addition, Chinese state banks have become more cautious about lending to projects under the strategy, which is China's plan to grow global trade. Some member countries, including Myanmar, Sierra Leone and Tanzania, are also reluctant to borrow large sums of money due to debt fears, while some have reduced planned borrowings or even cancelled unaffordable projects

U.S. Politics & Policy

A reasonably even-handed analysis: U.S. cooperation with the Syrian Kurds was an expediency without an exit plan...

The US played down Turkey's concerns about Syrian Kurdish forces. That couldn't last.

The policy of assisting a faction of Syrian Kurds, the YPG, to fight the Islamic State has been a ticking time bomb since it began under the Obama administration, in 2014.

The short-term imperative to combat the militant group, which is also known as ISIS, created a strategic contradiction with foreseeable consequences that are now on

painful display. Turkey, a NATO member, never accepted U.S. support for the group, which is directly linked to a terrorist organization that has long fought an insurgency against the Turkish state.

Nor did every politician now criticizing Trump — whose decision-making has been characteristically chaotic — think this alliance was wise in the first place. The main surprise here is that U.S. diplomats and military officers made this untenable situation work as long as it did.

I still think Pelosi has boxed herself into brining USMCA to the floor with the impeachment gambit, else she's pegged as #DoNothingDem...

[Trumka says fast action on trade pact with Canada and Mexico would be 'colossal mistake'](#)

A key labor leader has warned House Democrats not to expedite approval of a new North American trade deal, saying that the agreement remains far from complete and that a vote in coming weeks would be a "colossal mistake."

"If there was a vote before Thanksgiving, the agreement would be defeated," AFL-CIO President Richard Trumka told The Washington Post this week in an interview. Support from the 12.5 million-strong AFL-CIO would be critical in persuading many House Democrats to back the new trade deal, giving Trumka enormous sway in negotiations.

Trumka's comments come as the U.S. Chamber of Commerce pushes for a vote by Thanksgiving. Republican lawmakers and Trump administration officials are also trying to ramp up pressure on House Democrats to get the deal done

I agree with Sumner – the Fed is not that far off where they need to be at this point...

[Steady as she goes - TheMoneyIllusion](#)

The fact that the Fed is cutting rates despite the low unemployment rate is actually a good sign; it's an indication that the "market" part of market monetarism is increasingly taken seriously within the Fed. If only they had done so in 2008.

While I lean in a "dovish" direction at the moment, I also believe that many people are too dovish. Policy is not far off course, despite yield curve inversion. This is pretty close to what monetary stability looks like.

