



There is No QE

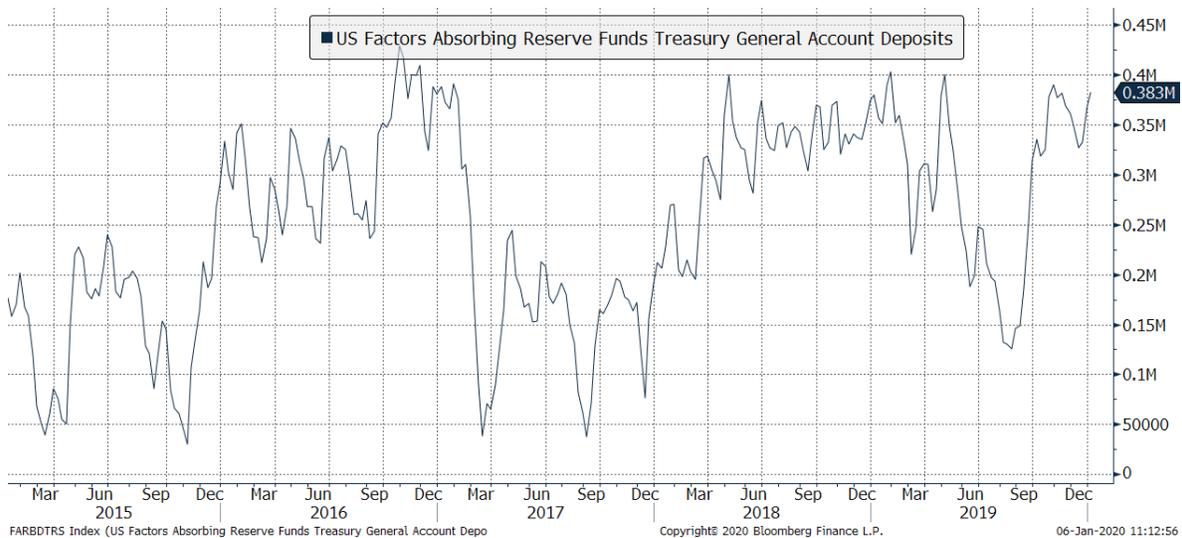
Happy New Year!

I'll have an update on the Q1 reflation trade later in the week. I remain very bullish risk assets, with an emphasis on EM, for a number of reasons, **none of which are related to Fed balance sheet activity.**

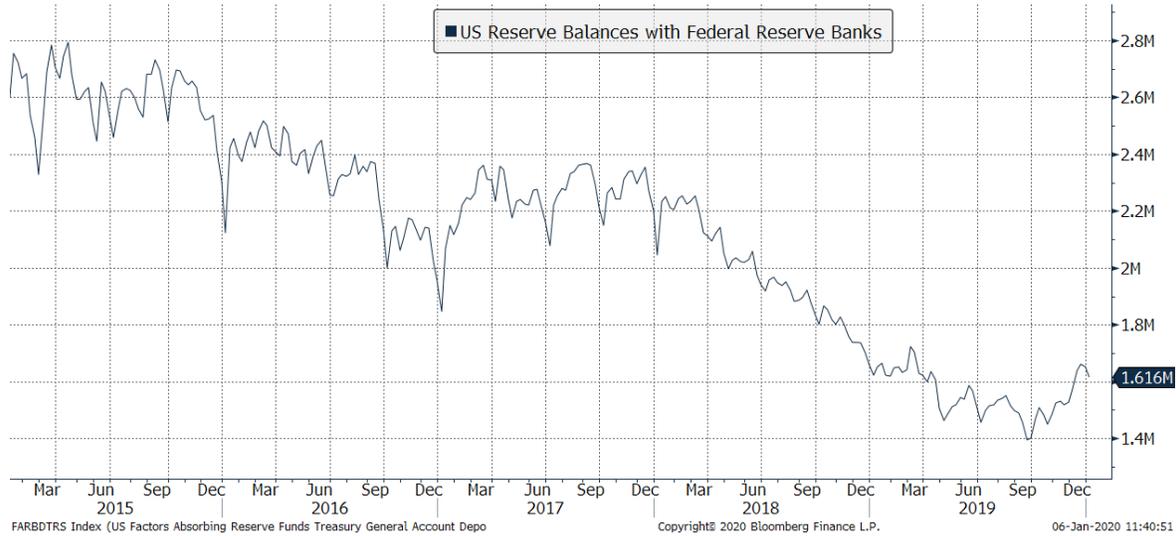
Today let's quickly dismiss the disconcertingly widespread argument that the Fed is "pumping up asset prices" with QE, and make sure we get off on the proper analytical footing in 2020.

There has been no QE in the dimensions that are relevant to asset markets: the level of bank reserves and the degree of duration removed from the market.

Here is the volume of funds in the Treasury General Account at the Fed – a **draining mechanism**. When the Treasury runs this account down (as it did for much of Q2) it is injecting funds into the system. **When the Treasury funds this account, it withdraws reserves from the system.** From August through October the Treasury Dept. effected a "quantitative tightening" of over \$250bn:



That "Treasury QT" operation pushed outstanding bank reserves to below \$1.4T in September, which we now know to **below the level of effective required reserves** around regulatory maintenance periods.



Criticism of the Fed for being asleep at the switch while this was unfolding is fully justified. Criticism for their waking up just before the train careened off the tracks is not.

All they've really done since is to offset the "Treasury QT" with Repo Agreements (to be unwound gradually in coming months in favor of increased holdings of T-Bills).

Federal Reserve: Simplified Balance Sheet

	8/15/2019	1/2/2020	Change
Total Assets	3,831,662	4,208,477	376,815
Securities Held	3,711,748	3,739,935	28,187
Other	119,914	226,216	106,302
Repurchase Agreements	0	242,326	242,326
Liabilities	3,831,662	4,208,477	376,815
Currency in Circulation	1,747,729	1,805,947	58,218
Treasury General Account	129,957	382,553	252,596
Other Factors Absorbing Funds	403,570	404,131	561
Total Factors Absorbing Funds	2,281,256	2,592,631	311,375
Reserves Balances	1,550,406	1,615,846	65,440

Since mid-August, Fed Repos merely offset the Treasury Department's unwitting draining operation, leaving Reserve Balances up by a paltry \$65bn.



Yes, the Fed will probably continue to buy T-bills to re-expand the balance sheet, and the pool of available reserves, by a few hundred billion Dollars in order to increase the excess reserves cushion over the now uncertain level of “regulatorily-required” reserves. With T-bills trading roughly flat to IOER, this should be of absolutely no interest to anyone.

Quantitative easing is designed to remove duration from the market and to increase the degree of monetary liquidity. Recent and prospective balance sheet operations do neither.

There is no QE and Fed balance sheet operations have nothing to do with the risk asset rally.