Big Time Monetary Stimulus

Our dear friend Marty Zweig coined the phrase “Don’t fight the Fed.” It would seem like good advice for investors today to apply what central banks around the world are doing and are likely to continue to do. Global Short Rates are likely to decline to 1.75% or below by the end of this year.

With the mfg PMI for prices down to 50.6%, a significantly inverted yield curve in the US is probably a risk we should not be running.

US retail gasoline peaked in early Oct of last year at $2.92. Judging by gasoline futures on Wednesday, retail prices will be down to $2.40 in early Oct of this year, an -18% y/y decline.
Commodity prices bleed into core (see charts below).
With WTI down -22% y/y and the GSCI down -16%, the core PCE is likely to move further away from +2.0%.
Why Test The Theory?

Bullard said yesterday that he’s not interested in testing the theory that “this time is different” with regard to the yield curve inversion.

With the global economy showing many signs of weakness, a significantly inverted yield curve in the US is probably a risk we should not be running.

1. US manufacturing recession begins.
2. India may have entered ‘quasi-recession’ as growth plummets.
3. China’s current GDP growth is likely less than 6%.
4. UK is on course for a recession.
5. Japan's exports slip, sales to China drop as recession fears grow.
6. Germany on brink of recession as business confidence nosedives.
7. Hong Kong on brink of recession as protests and trade war take toll.
Why Test The Theory? Contd

With a trade war escalating, etc, why would the Fed want to test the theory that “it’s different this time?” In the past, when the yield curve was inverted, eg, in 2006-2007, almost everything seemed fine. Because the economy is fine as inversions unfold, there is a tendency to think “it’s different this time”, ie, that the inversion is giving a false signal. In any event, Krishna Guha expects the Fed to cut -25bp in both Sep and Oct.

When the S&P peaked in Oct 2007, the yield curve had already been significantly inverted. The svc PMI in Oct 2007 was 53.5%, about what it is today. Real GDP growth in 4Q was +2.0% y/y.
Why Test The Theory? Contd

With the mfg PMI down to 49.1%, a significantly inverted yield curve in the US is probably a risk we should not be running.
Setting The Stage For Improvement

Mtg rates have declined significantly and are likely to decline further. As a result, refi has increased significantly and is likely to increase further. This is likely to help the economy improve.
Eurozone Bottoming?

We doubt that Eurozone economic activity is bottoming. EVRISI survey of Europe cos sales is still declining. But these two Eurozone readings reported today suggest a bottoming.
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