

# AquilaFlash



## Monetary policy fireworks of the ECB

**The ECB has further eased its monetary policy. President Trump would like to see the Fed also aggressively relax and demands negative interest rates. China and the US are trying to create a good mood for the upcoming negotiations by "showing signs of good will". We think small progress and further relaxation are possible.**

### **Key rate cut and resumption of QE**

The ECB lowers its key interest rate from -0.4% to -0.5%. In addition, bond purchases will be restarted. From November, bonds worth € 20 billion will be bought each month.

At the same time, the forward guidance became even more "aggressive". Better conditions for long-term credit should support the European banking system.

The ECB has thus delivered roughly what the consensus expected. According to Reuters, economists forecasted a 10-bp interest rate cut, € 30bn of bond purchases and ECB credits to European banks, and a promise to keep interest rates "even longer", Nevertheless, the market influence should be positive in the short term.

### **FED is now under greater pressure to act as well**

As will be explained later, the FED is pressurized to also stimulate more. At the same time, the trade conflict with the US could be exacerbated by these measures.

### **Consequences of negative interest rates**

Negative interest rates do not necessarily have to support economic activity. The standard theory assumes that with constant cash flow lower interest rates lead to a higher current value of future cash flows and therefore more investments and consumption. If, however, interest

rate cuts are understood by market participants as a "distress signal", in the sense of "My God, there is a threat of economic downturn or worse", interest rate cuts can even have a counterproductive effect, because then market participants expect falling cash flows.

The area of negative interest rates increasingly jeopardizes the existence of the European banking system or the survival of cash. If key interest rates are pushed even further into negative territory, more and more banks will also have to charge interest on smaller savings and current accounts, as cross-subsidization by other business units is no longer sufficient to avoid losses and ultimately bankruptcy. This would then lead savers to withdraw their deposits and hoard cash.

In order to prevent this avoidance of negative interest rates and to continue to enable credit creation by the banks, cash would have to be abolished / banned.

The low-interest-rate policy is leading to ever more uneven distribution of wealth, as it leads to very high equity, bond and real estate prices.

### **FED will "retaliate"**

Economic stimulus from a weak euro is also unlikely to materialize as the Fed is likely to "catch up". The US will not accept US dollar appreciation. Thus, any additional interest rate cut, any additional expansion of a central bank's balance sheet, is equivalent to extortion from all other central banks. The expansive monetary policy of the ECB annoys President Trump. At the same time, he is "jealous" and desperately longs for a "Super Powell" that can compete with "Super Mario".

### **President Trump increases pressure on the Fed**

This Wednesday, President Trump demanded that the Fed, like the ECB, cut its key interest rates into negative territory. Representatives of the Fed have already rejected this. The economy is running too well. The measures demanded by President Trump are absurd. The US unemployment rate remains at a record low and the weakening of the US economy in recent quarters is primarily the result of aggressive US foreign trade policy. President Trump's aim is to prevent any economic downturn and a baisse before the US presidential elections. But it is also about financing the numerous electoral gifts (tax cuts, "subsidies of selected groups") and the government deficit, which is completely out of control.

### **US and China try to spread good mood for the upcoming negotiations**

President Trump announced on Wednesday that he would delay the increase in import tariffs from 25% to 30% on \$ 250 billion worth of goods "for a short time from 1 to 15 October". China had previously announced that it would levy no additional tariffs on some US products, including cancer medicines. In addition, Chinese companies are required to expand the purchase of agricultural products from the United States. Both sides are trying to spread a good mood for the upcoming negotiations in mid-October. Mutual "gestures of goodwill" should also ensure a good mood in the financial markets in the short term. We believe that small progress and further relaxation are possible, but do not expect a major breakthrough, as the basic philosophical positions are too far apart and the fundamental conflict, "the struggle for world power", remains unresolved and will continue to be resolved by all means.

### **Contact:**

Thomas Härter, CIO, Investment Office  
Tel.: +41 58 680 60 44