Global Financial Crises 10 Years On - How Resilient are We Now?

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Remarks at the 28th Vienna Roundtable
OeKB Reitersaal

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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

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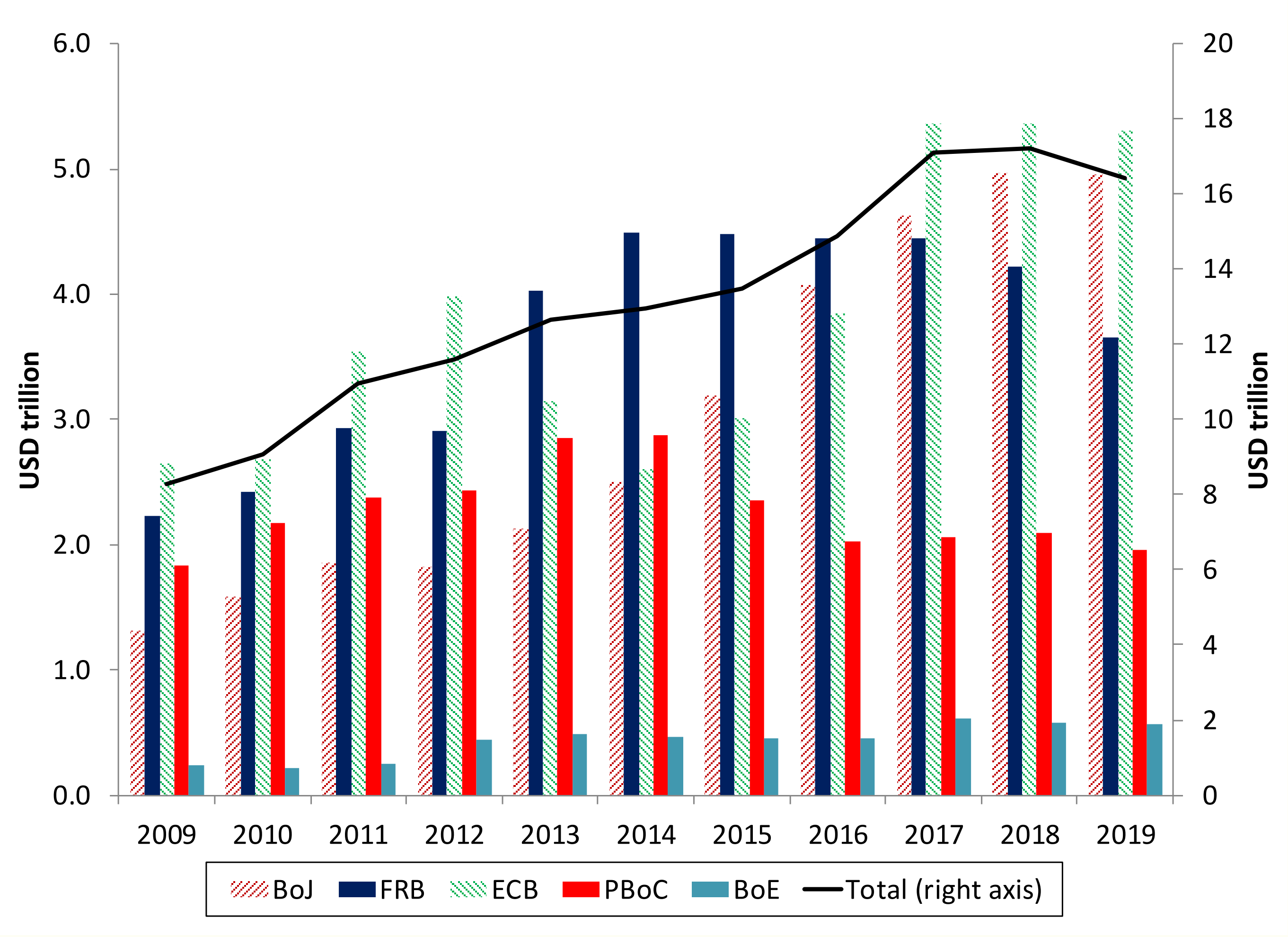
Major Central Banks: Stock of Liquidity



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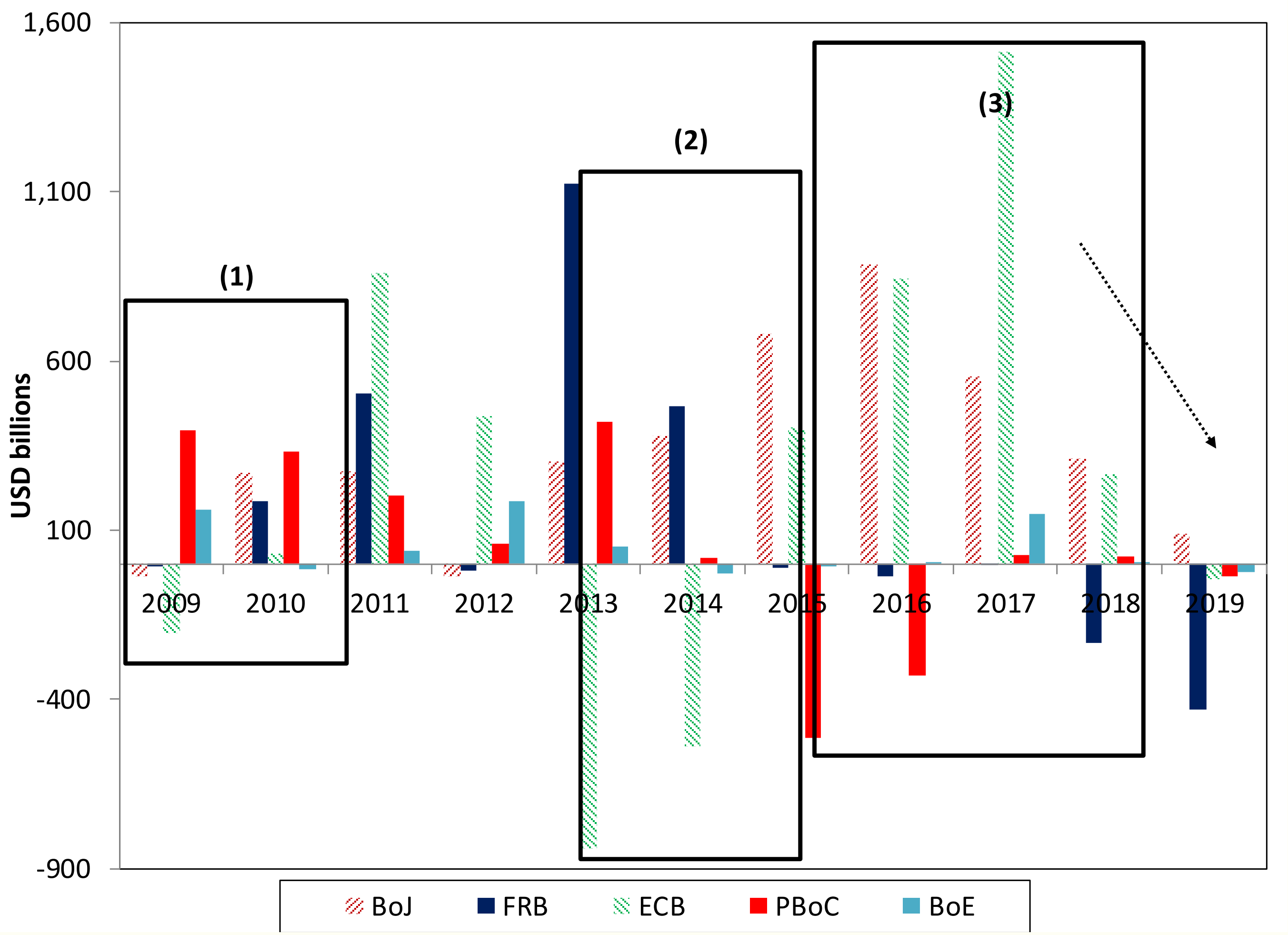
Source: Federal Reserve Board, European Central Bank, Bank of Japan, People's Bank of China, Bank of England, and Center for Financial Stability.

Major Central Banks: Flow of Liquidity



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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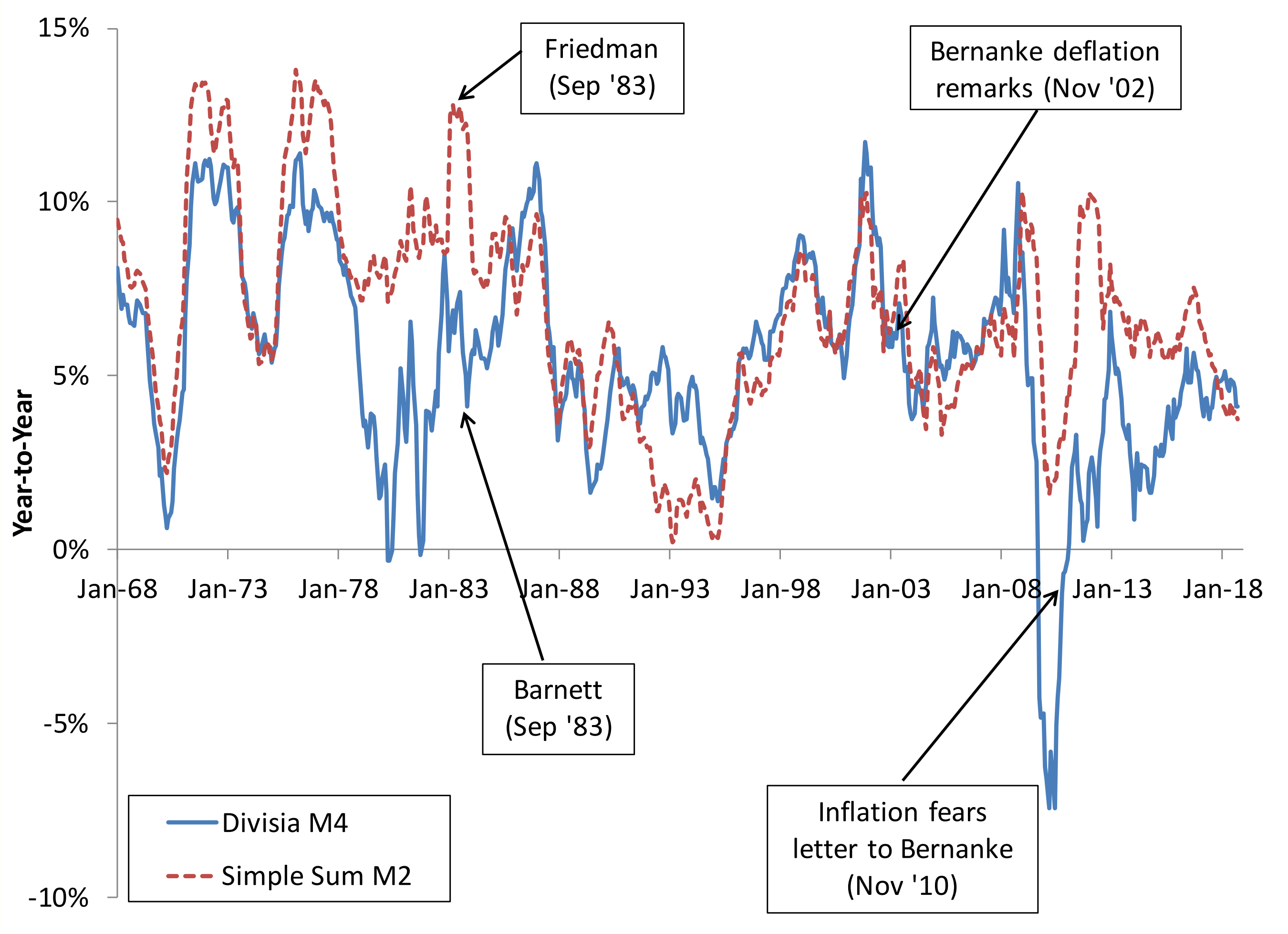
Why CFS Divisia Money Matters for Markets, the Economy, and Policy



Source: Federal Reserve Bank of St. Louis and Center for Financial Stability.

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1/ Cyclical peak-to-trough in months.

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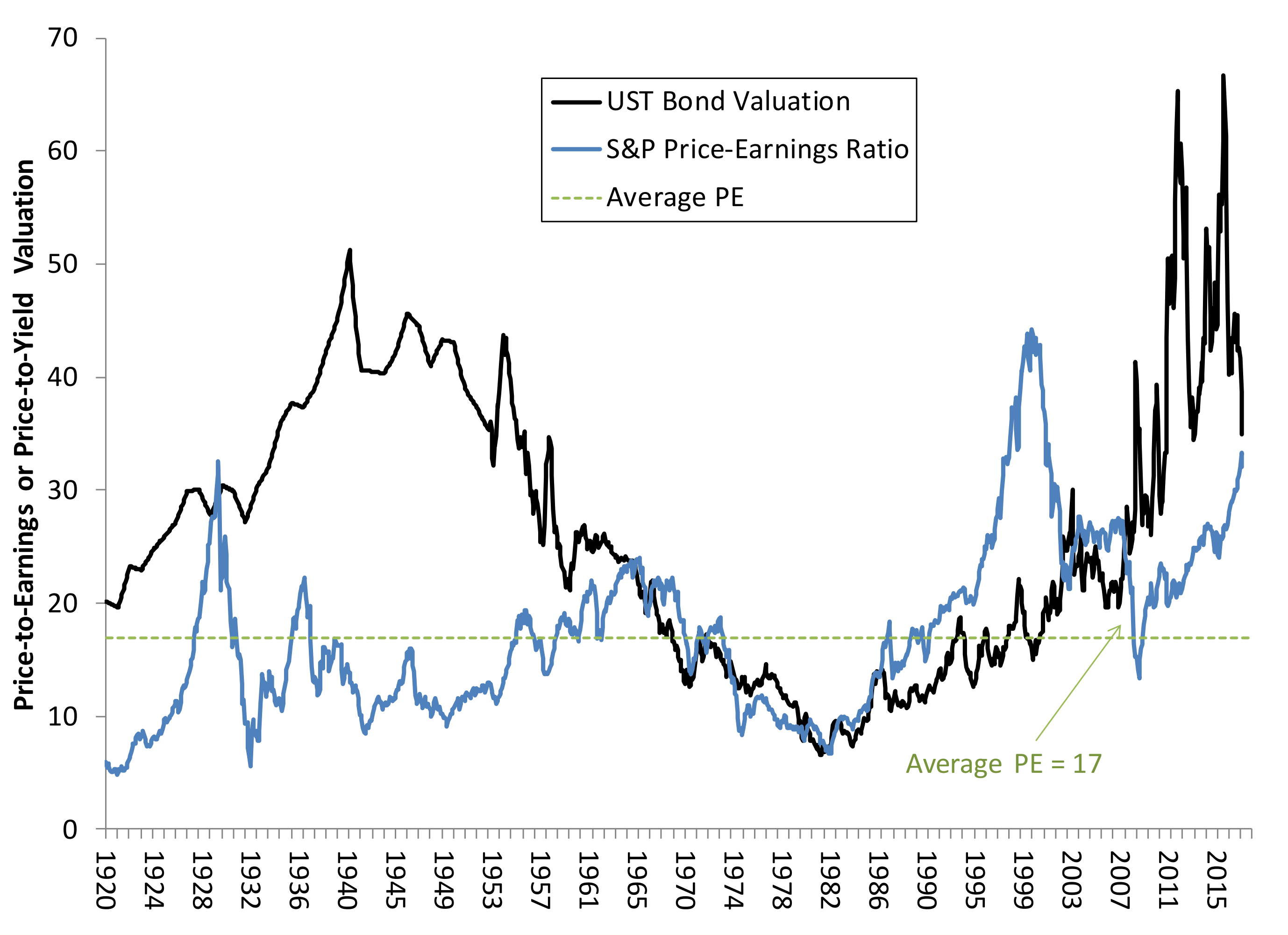
Policy Driven Distortions in Debt and Equity Markets



Source: Robert Shiller (Yale University), Bloomberg LP, and Center for Financial Stability.

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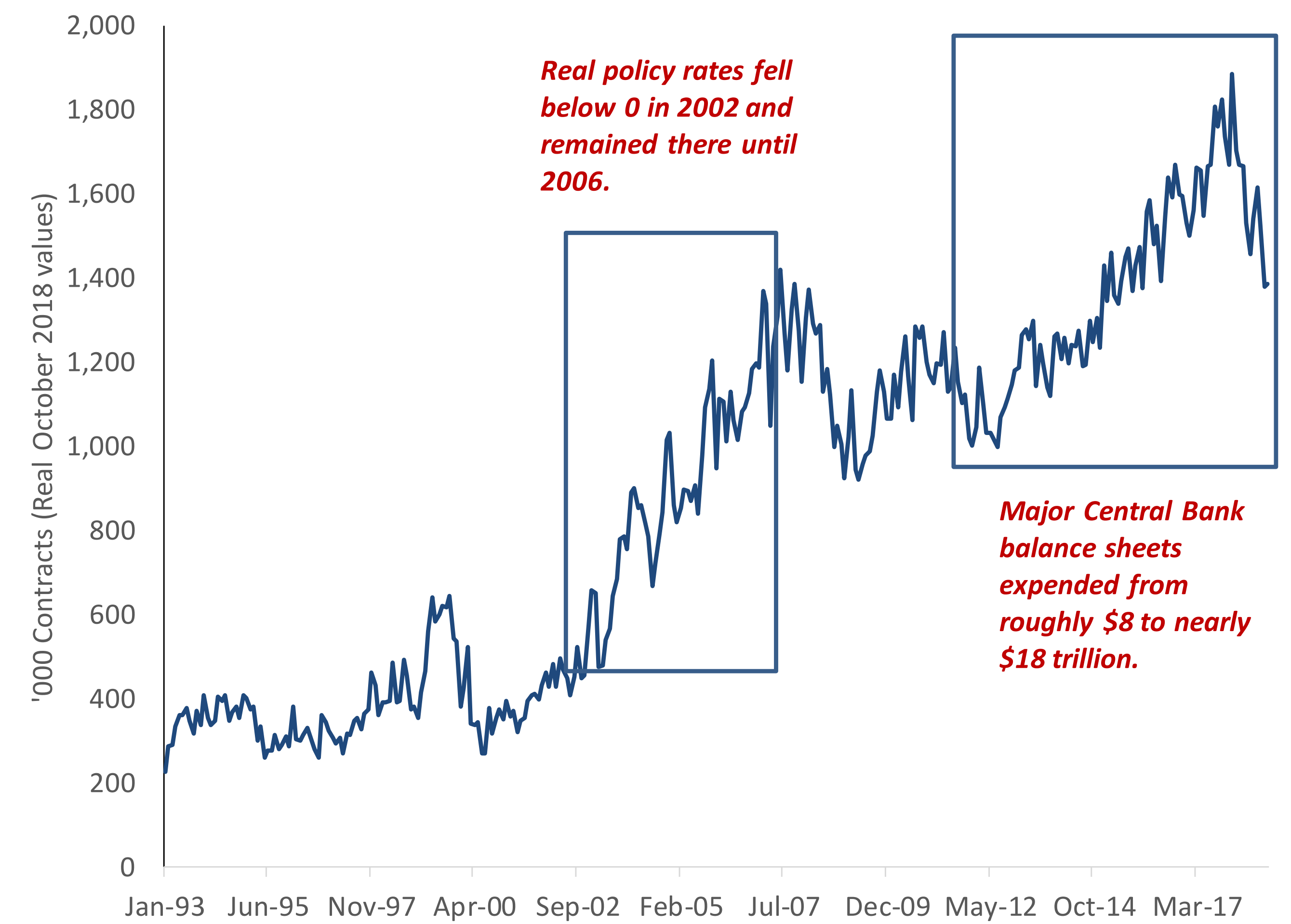
Accommodative Monetary Policy spurs Speculative Investor Behavior



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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1/ Cyclical peak-to-trough in months.

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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.

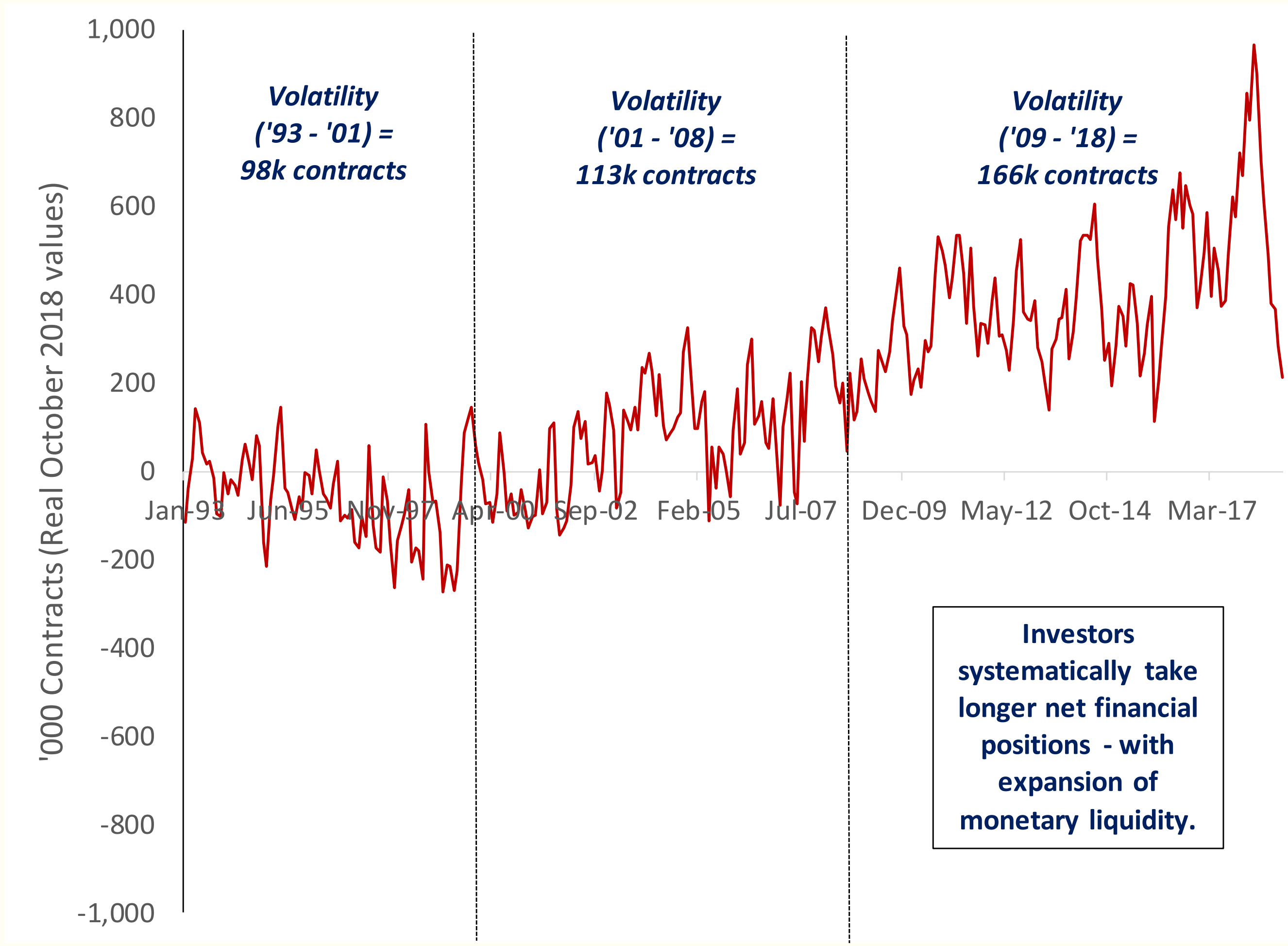
U.S. financial regulators would be well advised to ease restrictions that and expertise to the table to organize support for broken markets.

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.



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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