



Capital
Markets

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The Daily Deck

Chop off the tail of uncertainty

Given where Treasuries are sitting, nobody should be surprised if the Fed came out and cut 100bps to the 0-0.25 lower bound. As anyone who knows our work well appreciates, we think that cutting rates will have virtually zero economic impact in this backdrop. But, if cutting rates to the ZLB allows the Fed to show they are at “max help” and places more of a burden on fiscal to step in, then they should get on with it.

At that point, we would then look for coordinated action between the Fed and Treasury. Markets are reflecting an extraordinary level of uncertainty and the only thing that stems this tide is coordinated action to deal with the actual and potential cash flow crunch to US companies from the COVID-19 fallout. Roll out Powell and Mnuchin together for a presser. If there is genuine fear out there about this virus then have these two step to a microphone and say something about what they are going to do.

This is not a traditional economic slowdown where the end-point is elusive. Indeed, most people think that COVID-19 will be dealt with and under control by summer time. Thus it is paramount to deal with the potentially very substantial cash flow shock to corporates in the meantime.

Bridge loans for corporates and small businesses perhaps managed by the Fed (through the banking system) and backed by the Treasury would be a start. This, incidentally, also helps the frackers, which are likely to be under significant duress as oil collapses. A corporate tax moratorium (again, low cost, high impact that we highlighted last week) would be another layup. What is paramount right now is chopping the large tail of uncertainty with regards to the COVID-19 impact.

Households were in fantastic financial position heading into this. Thus the risk there is one of job losses. But this again is directly tied to the ability of companies under stress to deal with the cash flow shock. Solving that from the fiscal standpoint solves the risks of layoffs. Companies are loathe to lay off workers in the midst of what was an ultra tight labor market ahead of COVID-19. Unlike a traditional recession, the inclination here is to hunker down and get through the cash crunch, not look for cutting back operating expenses.

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