A LOT OF BIS & A BIT OF STEVE KEEN
DON'S BLOG 2017.09.18

The bank for international settlements (BIS) is one of the organizations of which I have much respect. The primary reason for that respect came from their former head, William White. He no longer is there and maybe that's the reason I found the following article a setback in my respect. It has to do with inflation which they proclaim a mystery of why it's not higher because of low interest rates and a pickup in global growth. Please note the following article excerpt from Reuters concerning the inflation "problem":

> The conundrum of stubbornly low inflation despite a pick-up in global growth and continued monetary stimulus is a "trillion dollar" question, the umbrella body for the world's leading central banks said on Sunday.
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> The Bank for International Settlements (BIS) said in its latest quarterly report that cheap borrowing rates and the rare simultaneous expansion of advanced and developing economies are driving financial markets higher, with signs of "exuberance" starting to re-emerge.
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> U.S. corporate debt is much higher than before the financial crisis and a drop in the premiums investors demand for riskier lending has boosted sales of so-called covenant-lite bonds offering high yields.
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> The BIS said this raises a question over the potential for another crisis if there is a significant rise in interest rates. The body has called for a gradual return to higher rates, though central banks are being tentative because of persisting low inflation.
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> "It feels like 'Waiting for Godot'," said Claudio Borio, the head of the monetary and economic department of the BIS, referring to a play in which the main characters wait for someone who never arrives.
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> But the BIS says no one has yet worked out why inflation has remained so subdued while economies have approached or surpassed estimates of full employment and central banks have provided unprecedented stimulus.
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> "This is the trillion-dollar question that will define the global economy's path in the years ahead and determine, in all probability, the future of current policy frameworks," Borio said.
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> "Worryingly, no one really knows the answer."

I, along with others do know the answer. There is a shortage of nothing except brains on one hand and on the other there is too much debt service and not enough income on the part of some 80% to 90% of the world's population. And what's more, that will not change under current public policy. It's just as simple as that.

The second half of the same article (shown below) does bring up what I really worry about, and that's of course a big surprise—more and more debt, and higher asset valuations. You see, that's where the inflation is: asset prices and not day to day price levels of goods and services.

> The report also contained a study that showed global debt could be under-reported by about $13 trillion because traditional accounting practices exclude foreign exchange derivatives used to hedge international trade and foreign currency bonds.
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> The main focus of the report, though, was the lack of inflation, the heady rally in financial markets, their ability to shrug off geopolitical tensions and what the BIS called the "remarkable" low levels of market volatility.
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> "We do not fully understand the factors at work. But surely the unprecedented gradual pace of monetary policy normalization has played a role," Borio said.
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> "All this puts a premium on understanding the 'missing inflation', because inflation is the lodestar for central banks."
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> The BIS, as normal, used its report to flag potential areas of risk that may be developing.
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> Since the global financial crisis, global debt in relation to GDP has continued to rise. Deleveraging has not really occurred and where private debt levels have adjusted, at least to some extent, public debt has taken over.
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> "A defining question for the global economy is how vulnerable balance sheets may be to higher interest rates."
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> Certain indicators do also point to vulnerabilities. Property development, a traditional bubble blower, is helping to fuel booms parts of Asia. Debt-service ratios, meanwhile, are only so low because interest rates have fallen so much.
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> "There is a certain circularity in all this that points to the risk of a debt trap," the BIS said.
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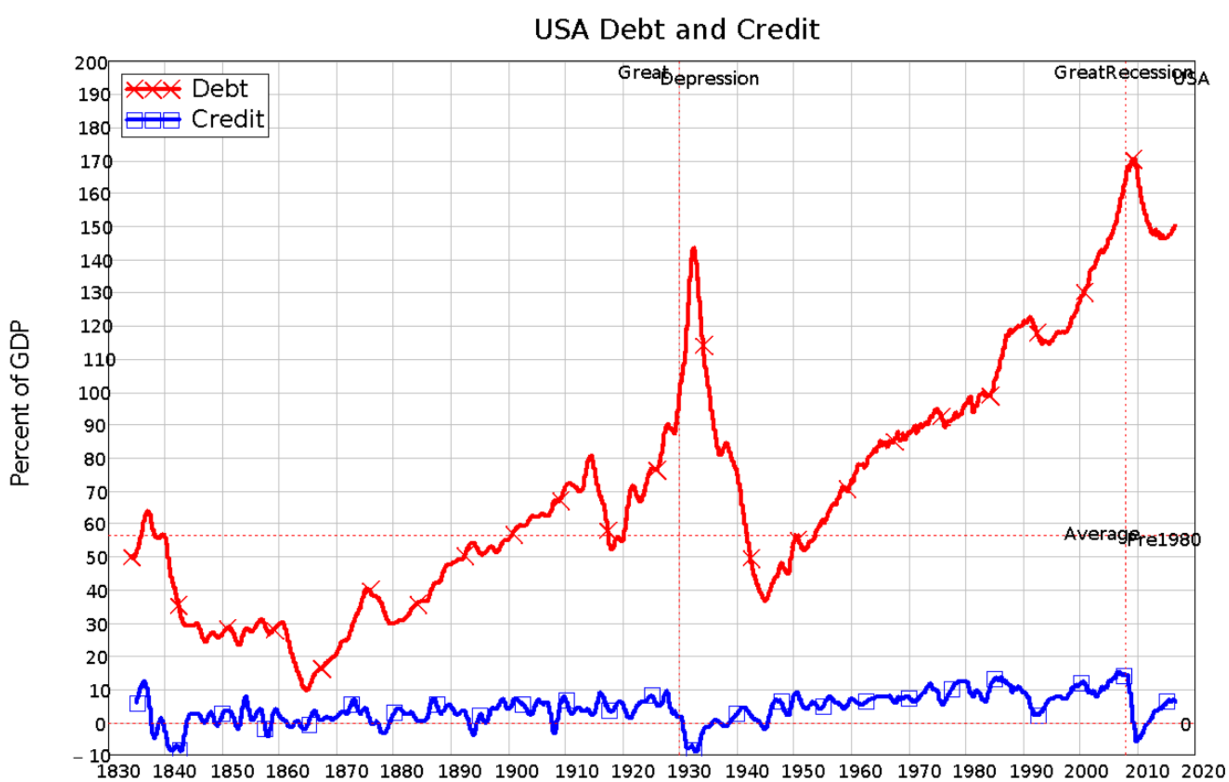
> The protracted decline in interest rates to unusually low levels, regardless of the strength of the underlying economy, creates the conditions that complicate their subsequent return to more normal levels, it added.

“Against this backdrop, the increase in the percentage of firms unable to cover their interest payments with their earnings -- so-called ”zombie“ firms -- does not bode well.”
http://www.reuters.com/article/us-bis-report-inflation/muted-inflation-a-trillion-dollar-puzzle-says-bis-idUSKCN1BS0OY

My old friend Steve Keen sent me a copy of his latest chart on US private debt and credit, and is shown below. The reason I have been so wrong in expecting a recession at any moment over the last five or six years is the debt to GDP ratio, along with the rate of credit increase. Both have not gotten to extremes as of yet in his mind, and it makes a lot of sense. One just really doesn’t know when that extreme takes place. So, expect more of the same for now.

What will we get from the Fed meeting this week? My guess is no rate increase and an announcement of the Fed stopping the reinvestment of treasury run offs beginning next year, unless something changes.



BIS and US Census Bureau normalised data