



University of Essex

# Financial Systemic Risks Post Covid 19

## *Ghosts of Crises Past*

# I. Where are the infected/toxic assets ?

# II. More QE: Flogging dead  
Horses; Carry trades

#III. Severe Liquidity Problems

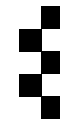
#IV: Fear Deflation not Inflation



**Professor Sheri Markose**  
**Economics Department**

# **Ghosts of Crises Past I: Parallel Between Covid 19 and GFC**

- Lockdown of all the population of multi-trillion economies: a blunt instrument & extremely destructive
- Lack of information and preparedness to isolate Covid-19 infected persons
- Digital competencies in test, track, trace lacking in advanced western economies (Insufficient Tech savy in Govt. And delivery of policy )
- **The Country that Beat the Virus: What Can Britain Learn?** (Channel 4 May 2020) was an in-depth look at how [South Korea has dealt with Covid-19](#)
- Analogous to GFC when toxic sub-prime assets co-mingled in Collateral Debt Obligations – crashed markets: *Run on the Repo*



# Ghosts of Crises Past II: Repeat QE and Zero Interest Rates

- I'm all for Targeted and Time limited Interventions : Treasury meeting 80% of wage bills in Furlough schemes to keep economy in *suspended animation till economy picks up after lockdown over*

Otherwise we face a **an Unemployment Precipice**

- **Get cash directly to SMEs :**
- **Generic QE** is flogging a dead horse

My paper on QE and *Why Banks Do Not lend to Businesses (JEBO, 2019)*

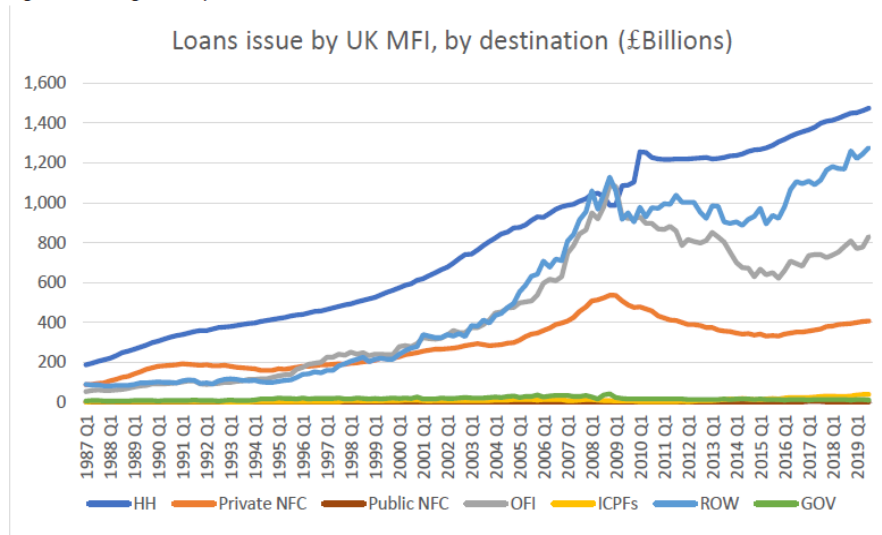
*Risk Weights penalize lending to SMEs ; Corporates switch to issues debt (bonds) buying back shares*

- QE by which high quality liquid assets are withdrawn from circulation

- Pumps up asset bubbles : Exacerbates income inequality

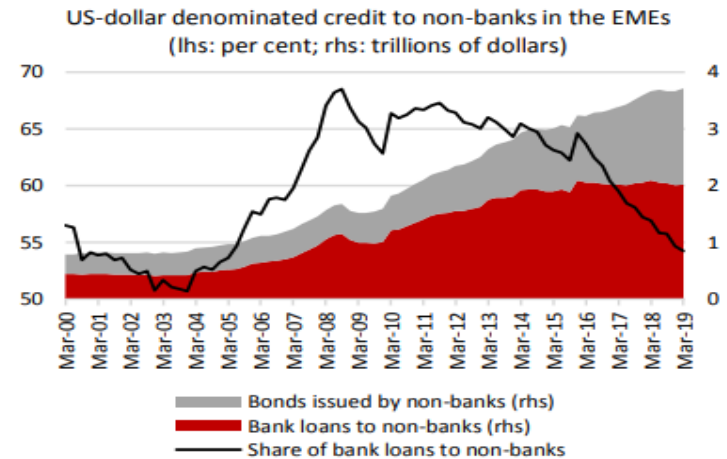
# Accelerating Carry Trades: Where is QE money going ? ROW

Figure 7. Banking Loans by sector



Source: Office for National Statistics.

Panel B



Source: BIS, Global Liquidity Indicators

The dollar debt of non-banks outside the United States is at a new record (\$4-5 Trillion): currency mismatches and leverage in the private sector have increased. The dollar funding of non-US banks looks fragile. Dec 2019 Report from the Robert Triffin Institute

Panel B EMEs Dollar Loans to non-Banks

# Ghosts of Crises Past III Flight to Cash & Severe Liquidity Crises in repo

- Corporates heavily leveraged going into Pandemic

Global debt on non-financial corporations stood at \$71 trillion by the end of 2018 up 15% from 2008 and represents 93% of global GDP (<https://hbr.org/2020/04/managing-the-liquidity-crisis> )

- Bears are shorting UK companies

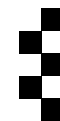
- Non-performing loans are piling up on bank balance sheets

- Many will argue that Fed/BoE/ECB by proactively becoming lender of last resort before liquidity crunch is on us

- Misfiring Liquidity/ Repo Markets

Ironically I have raised the alarm on insufficient HQLA which are now on central bank balance sheets

Liquidity Hoarding; Negative Repo Rates

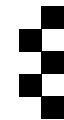


# The Dilemma

- Curved Ball : New Govt Debt for stimulus drains liquidity and crowds out Private Sector spending
- QE central bank purchases of securities , drains repo collateral and piles up central bank reserves

*Which market will give ? Imploding Carry trades  
Or just decades of misery ?*

- Govt Debt to be paid off by future tax increases and austerity ???



# Concluding Remarks

# Is Inflation a problem Post Covid with all the Fiscally funded purchasing power?

Not in cashless economies where cash purchases are being driven out almost completely in retail

# Countering deflation important with anemic demand and off the wall unemployment rates

## References

- Fatouh, M., Markose, S. and Giansante, S., 2019. The impact of quantitative easing on UK bank lending: Why banks do not lend to businesses?. *Journal of Economic Behavior & Organization*, pp.1-26.

- Icard, A., Turner, P. Turner, Snoy, B. (2019), **MANAGING GLOBAL LIQUIDITY AS A GLOBAL PUBLIC GOOD** A REPORT OF ANRTI (Robert Triffin Institute)

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