4/24/13 Helicopter QE will never be reversed- Telegraph

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**Helicopter QE will never be reversed**

**Readers of the Daily Telegraph were right all along. Quantitative easing will never bereversed. It is not liquidity management as claimed so vehemently at the outset. It really is the same as printing money.**

**It would be better for central banks to put the money into railways, bridges, clean energy, smart grids, or whatever does most to regenerate the economy.**

By Ambrose Evans-Pritchard

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Columbia Professor Michael Woodford, the world's most closely followed monetary theorist, says it is time to come clean and state openly that bond purchases are forever, and the sooner people understand this the better.

"All this talk of exit strategies is deeply negative,"he told a London Business School seminar on the merits of Helicopter money, or "overt monetary financing".

He said the Bank of Japan made the mistake of reversing all its money creation from 2001 to 2006

once it thought the economy was safely out of the woods. But Japan crashed back into deeper

deflation as soon the Lehman crisis hit.4/24/13 Helicopter QEwill never bereversed- Telegraph

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"If we are going to scare the horses, let's scare them properly. Let's go further and eliminate government debt on the bloated balance sheet of central banks,"he said. This could done with a flick of the fingers. The debt would vanish.

Lord Turner, head of the now defunct Financial Services Authority, made the point more delicately. "We must tell people that if necessary, QE will turn out to be permanent."

The write-off should cover "previous fiscal deficits", the stock of public debt. It should be "post-facto monetary finance".

The policy is elastic, for Lord Turner went on to argue that central banks in the US, Japan and Europe should stand ready to finance current spending as well, if push comes to shove. At least the money would go straight into the veins of the economy, rather than leaking out into asset bubbles.

Today's QE relies on pushing down borrowing costs. It is "creditism". That is a very blunt tool in a

deleveraging bust when nobody wants to borrow.

Lord Turner says the current policy has become dangerous, yielding ever less returns, with ever worsening side-effects. It would be better for central banks to put the money into [loan, take equity position in? give ?] railways, bridges, clean energy, smart grids, or whatever does most to regenerate the economy.

The policy can be "wrapped" in such a way as to preserve central bank independence. The Fed or the Bank of England would decide when enough is enough, or what the proper pace should be, just as they calibrate every tool. That at least is the argument. I merely report it.

Lord Turner knows this breaks the ultimate taboo, and that taboos evolve for sound anthropological reasons, but he invokes the doctrine of the lesser evil. "The danger in this environment is that if we deny ourselves this option, people will find other ways of dealing with deflation, and that would be worse."

A breakdown of the global trading system might be one, armed conquest or Fascism may be others - or all together, as in the 1930s.

There were two extreme episodes of money printing in the inter-war years. The Reichsbank's financing of Weimar deficits from 1922 to 1924 - like lesser variants in France, Belgium and Poland - is well known. The result was hyperinflation. Clever people made hay. The slow-witted - or the patriotic - lost their savings. It was a poisonous dichotomy.

Less known is the spectacular success of Takahashi Korekiyo in Japan in the very different circumstances of the early 1930s. He fired a double-barreled blast of monetary and fiscal stimulus together, helped greatly by a 40pc fall in the yen.

The Bank of Japan was ordered to fund the public works programme of the government. Within two years, Japan was booming again, the first major country to break free of the Great Depression. Within three years, surging tax revenues allowed Mr Korekiyo to balance the budget. It was magic.

This is more or less the essence of "Abenomics", the three-pronged attack on deflation by Japan's new premier and Great Power revivalist Shinzo Abe.

Stephen Jen from SLJ Macro Partners says Western analysts have been strangely slow to understand the breathtaking scale of what is under way. The Bank of Japan is already committed to bond purchases of $140bn a month in 2014. This is almost double the US Federal Reserve's net purchases (around $75bn a month), and five times as much as a share of GDP.

Prof Woodford and Lord Turner both think the Fed has already begun to monetise America's deficits, though Ben Bernanke has been studiously vague whenever pressed in testimony on Capitol Hill. These are early days. It is tentative and deniable.

The great hope is that this weird episode will soon be behind us, and that such shock therapy will never be needed in the end. If stock markets tell the truth, the world economy is already healing itself. Another full cycle of global growth is safely under way.

But stock markets are a bad barometer at the onset of every crisis, not least the blistering rally of late 1929, a full year after the world economy had tipped into commodity deflation.

The Reuters CRB commodity index has been falling steadily for the past six months. Copper futures

have dropped 10pc since mid-February. This is nothing like the early months of the great global boom

a decade ago.

The bull case rests on US recovery, a seductive story as the housing market comes back to life and the shale boom revives the US chemical industry.

Yet the US money supply figures are no longer flashing buy signals. The M2 money stock has contracted over the past three months, and M2 velocity has dropped to the lowest ever recorded at 1.54.

The country must navigate a fiscal squeeze worth 2.5pc of GDP over the rest of the year, arguably the biggest fiscal shock in half a century. Five key indicators have been soft over the past week, with the ADP jobs index coming in much weaker than expected on Wednesday. Growth is below the Fed's "stall speed" indicator, an annualized two-quarter rate of 2pc.

The buoyancy over the past quarter has been flattered by a collapse in the US savings rate to preLehman depths of 2.6pc, and while falling saving is what the world needs, it is not what America needs. Thrifty Asians are the people who must spend if we are to right the collosal imbalances in the global system.

The world savings rate is still climbing to fresh records above 25pc. For all the talk of change in China, Beijing is still pursuing a mercantilist policy. It is still flooding the world with excess goods. It is still shoveling cheap credit into its shipbuilding industry, adding to the glut. It is still keeping its solar industry on life-support.

China remains chronically reliant on global markets. Given that its trade surplus is rising again, it is

questionable whether China is adding any net demand to the world.

The eurozone, Britain and an ever widening circle of countries in Eastern Europe and the Balkans are mired in recession. Growth is expected to be just 2pc in Russia and 3pc in Brazil this year.

My fear - hopefully wrong - is that recovery will falter over the second half, leaving the developed world trapped in a quasi-slump, a sort of grey zone of zero growth that goes on and on, with debt trajectories ratcheting up.

The Dallas Fed's PCE index of core inflation has already dropped to 1.1pc over the past six months. The eurozone's core gauge has fallen to 1.5pc. A dozen EMU countries already have one foot in deflation with flat or contracting nominal GDP. Another shock will tip them over the edge into a deflationary slide.

If Lord Turner's helicopters are ever needed, we can be sure that the Anglo-Saxons and the Japanese will steal a march, while Europe will be the last to move. The European Central Bank will resist monetary financing of deficits until the bitter end, knowing that such action risks destroying German political consent for the euro project.

By holding the line on orthodoxy, the ECB will guarantee that Euroland continues to suffer the deepest depression. Once the dirty game begins, you stand aside at your peril.

A great many readers in Britain and the US will be horrified that this helicopter debate is taking place at all, as if the QE virus is mutating into ever more deadly strains.

Bondholders across the world may suspect that Britain, the US and other deadbeat states are engineering a stealth default on sovereign debts, and they may be right in a sense. But they are warned.

This is the next shoe to drop in the temples of central banking.

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