Negative interest rates bad for savers, economy and banks!

18 Sept.—If he is not stopped, outgoing European Central Bank (ECB) President Mario Draghi's last major act will ensure the final destruction of the European economy in order to shore up the City of London's European Union project.

Against the opposition of 12 of the 25 governors on the ECB board, Draghi announced on 12 September that the interbank lending rate would move further into the negative realm, from -0.4 to -0.5 per cent, and that quantitative easing would crank up again at a rate of €20 billion per month, "for as long as necessary". In addition, the bank will continue reinvesting principal payments from maturing securities purchased by the asset purchase program in the past.

The bank also announced a two-tier rate system which would exempt banks that hold more capital than the minimum reserve ratio from being charged negative rates, to alleviate pressure on lenders. More accommodative terms were adopted for the Targeted Longer-Term Refinancing Operation (TLTRO) announced in March to shore up bank balance sheets.

The ECB announced "the need for a highly accommodative stance of monetary policy for a prolonged period of time", reiterating that it "stand[s] ready to adjust all of its instruments, as appropriate, to ensure that inflation moves towards its aim in a sustained manner". This is a commitment to pumping up collapsing asset bubbles, not to resurrecting the economy. Bolstering growth is critical to the advancement and function of the Economic and Monetary Union, Draghi added—which includes finalisation of the City of London's Banking Union and Capital Markets Union project. Draghi has been a key figure in the destruction of political and economic sovereignty enacted by the EU and single currency.

Echoing demands made at the US Fed's Jackson Hole meeting on 22-24 August, Draghi demanded governments play their part to prop up the dying system: "In view of the weakening economic outlook and the continued prominence of downside risks, governments with fiscal space should act in an effective and timely manner. ... All countries should reinforce their efforts to achieve a more growth-friendly composition of public finances."

A headline in German newspaper *Bild Zeitung* on 13 September blared that "Count Draghila is sucking our accounts dry. In his term we lost billions." The article continued: "The horror for German savers goes on and on." The German savings rate is nearly twice the European average. The low interest rates are hurting savers and pensioners, but are fueling a property boom, which includes a flood of foreign investment. (By contrast, when the People's Bank of China on 16 September lowered the required reserve ratio for Chinese commercial banks by 0.5 per cent, and a full 1 per cent for regional industry and manufacturing lenders, allowing them to create more credit, it raised the reserve ratio for real estate lending, restricting credit to the bubble.)

"Count Draghila" featured in the German newspaper Bild.

Negative rates turn usual processes upside-down. In a 21 August article for the *Irish Examiner*, Irish financial adviser and author Eddie Hobbs described the phenomenon: "There is no credible evidence that negative interest rates improve credit creation because its upside-down sensation scares consumers into hoarding and saving not borrowing and spending. A negative world drains liquidity from bond and money markets and makes banks more conservative in lending." Central banks will react by pushing even further into the negative domain and quantitative easing, or even more extreme versions of monetary policy, while debt-laden governments take on even more in attempted fiscal stimulus. But it will not work. All that was achieved by the stimulus after the last crisis was to inflate new bubbles, Hobbs argued.

Negative interest rates "crush banks", *Wolf Street*'s Wolf Richter said in a 21 August podcast, by distorting the pricing of risk. "So zero per cent interest rates and worse, negative interest rates, are terrible for banks for the long term. And because they're bad for banks, by extension, they're also bad for the real economy that relies on banks to provide the financial infrastructure so that the economy can function.

“Commercial banks need to take deposits and extend loans. That’s their primary function. This credit intermediation, as it’s called, is like a financial utility. One bank can be allowed to fail. But the banking system overall cannot be allowed to fail. That would be like the lights going out. So, there needs to be special regulations, just like there are regulations on electric utilities.”

Writing in the *Telegraph* on 22 August, British journalist Ambrose Evans-Pritchard quoted Professor Richard Werner, a German bank expert at Oxford University, saying that important banking functions were being crippled by negative rates: “It is wiping out the remaining 1,400 savings and community banks. For the last 200 years, these banks have been the backbone of German economic performance. It is thanks to this solid network of local lenders that Germany has its thriving *Mittelstand* of family firms. They provide 90 per cent of the credit for small and medium enterprises”, he said. Some had to merge or were forced into property speculation. “What the ECB is doing favours the big casino banks. It is going to ruin Germany in the end. It is criminal”, he concluded.

The German five-year bund is now at -0.93 per cent, meaning that investors pay 0.93 per cent a year for the privilege of lending to the German Government for five years, while the 10-year bund is shadowing the official central bank rate. For the first time ever Germany now offers a 30- year bond which pays no interest at all (zero per cent rate). Denmark has had a similar experience with seven years of negative rates; Jyske Bank is “selling” 10 year mortgages at -0.5 per cent per annum. (In the 1970s Switzerland went as low as imposing a -41 per cent rate on foreign deposits; see “Switzerland Tried Negative Rates in the 1970s. It Got Very Ugly” from Bloomberg.)

Central banks have begun to pass on the expense of holding cash. An August Bloomberg article reported that eurozone banks spend over €7 billion per year to park overnight funds at the central bank and their lending income is also being eroded. In August, two major Danish banks began charging -0.6 per cent for corporate clients holding deposits larger than US$1.1 million. Rates for retail customers are as low as (positive) 0.07 per cent in some cases, but a number of bankers have indicated they need to consider passing on negative rates to customers with smaller bank accounts, a topic also under discussion in Germany.

Many commentators have detailed the negative consequences of negative rates, one of the most recent being Huw van Steenis, a former adviser to Bank of England Governor Mark Carney. Writing 3 September in the *Financial Times*, he observed that “Like steroids, unconventional monetary policy can be highly effective in small dosages, but just as long-term usage of steroids weakens bones, so below-zero interest rates can weaken the financial system.”

Upon Draghi’s unilateral decision—a vote is apparently not necessary in the ECB forum—Austrian National Bank Governor Robert Holzmann admitted the idea that the new measures might be a mistake “definitely” crossed his mind. US President Donald Trump, however, called for continued rate cuts into the negative domain, as “other countries are already doing”. Former Fed Chairman Alan Greenspan, interviewed on CNBC on 4 September, observed that “it’s only a matter of time” before negative rates spread to the USA. JPMorgan Chase head Jamie Dimon is preparing the bank for negative rates. The Fed’s rate committee is scheduled to meet today (18 Sept.) and is widely expected to make a cut. On 17 September the Fed was forced to inject US$53 billion into the interbank lending market, following a sharp spike in the interest rate for overnight lending reminiscent of the 2008 credit crunch. It has pledged a further US$75 billion injection on Wednesday 18th.

As for Australia and New Zealand, as Bloomberg reported on 22 August, the two central banks that once eschewed extreme monetary policy are now “at the forefront of what appears to be a race to the bottom—where even interest rates at zero may not be far enough”. On 13 September Westpac Chief Economist Bill Evans told the *Australian Financial Review* that the Reserve Bank of Australia will likely have moved to some version of extreme monetary policy by February next year. Independent economist John Adams observed that this was why the Morrison government wanted to have its $10,000 cash ban in place by 1 January 2020, given the IMF’s insistence that negative interest rates won’t work without cash restrictions to stop people from pulling their money out of banks.

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