SMBC

SMBC Group

US Macroeconomics

March 17, 2023

Joseph Lavorgna, Chief US Economist | 212.610.1741 | joseph.lavorgna@smbcnikko-si.com

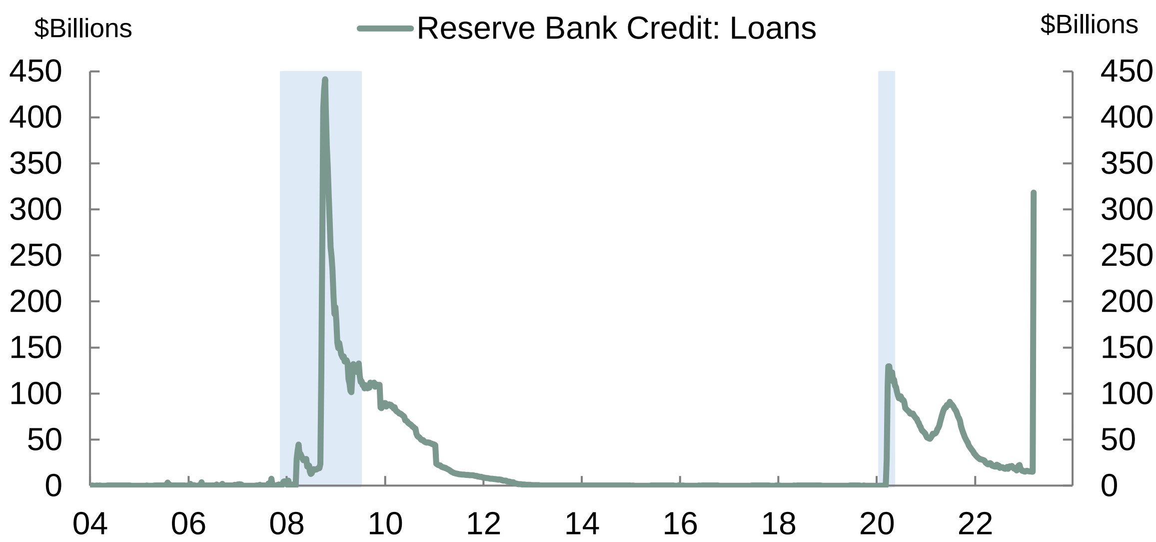
The Fed Just Did Massive QE

Last night the Fed published its H.4.1 release. This is the report that provides a weekly snapshot of the Fed's balance sheet for the week ending Wednesday. So, we have what the Fed balance sheet looks like as of March 15th and boy was it a doozy. **The Fed effectively just did $318 billion of quantitative easing (QE)**). Yes, you read it correctly. The Fed effectively added $318 billion in reserves to the financial system. It is no wonder that risk assets responded as they did. Once again, the system is awash in liquidity. This is big news, and no doubt increases the chances that the Fed stops quantitative tightening (QT) all together because the banking system has come to depend on ample reserves.

When the Fed makes loans through the discount window, they are counted as assets on its balance sheet. In the process, the Fed effectively creates money or reserves that banks can use. The loans the Fed made were nearly equally divided between "primary credit to depository institutions" and "other credit extensions" for those that want to find the line items for themselves on the balance sheet. According to the Fed, primary credit is available to generally sound depository institutions on a very short-term basis, typically overnight, at a rate above the target rate for fed funds. This past week's surge represents the creation of the new Bank Term Funding Program (BTFP). The other credit extension category was created during the 2008 financial crisis.

As shown in the chart below, **Fed loans (i.e., primary and other credit) increased $318 billion this week to the highest level since November 2008 during the height of the financial crisis**. But in weekly terms, this past week's surge was larger than anything seen during the financial crisis. This tells us that there was (and probably still is) tremendous pressure on the financial system as firms scrambled for liquidity. Moreover, when we look at reserve balances at the Fed, they soared $440 billion, effectively offsetting three-quarters of the past year's QT in just one week.

For our regular followers, this is not a surprise. **Unprecedented rate increases alongside an inverted curve foreshadowed a financial blowup of some sort**. But now that we have it, will the Fed continue on the course that got us here? We will find out this coming Wednesday. Current financial stability is tenuous.



Sources: Federal Reserve, Haver, SMBC Nikko

Disclaimer

This document has been prepared by SMBC Group (including, collectively or individually, Sumitomo Mitsui Banking Corporation, SMBC Nikko Securities America, Inc., SMBC Nikko Securities Canada, Ltd., SMBC Capital Markets, Inc., SMBC Leasing and Finance, Inc., JRI America, Inc., and SMBC Rail Services LLC) and is being furnished by SMBC Group solely for use by the client or potential client to whom such materials are directly addressed and delivered. SMBC Nikko Securities America, Inc. ("SMBC Nikko America") is a US-registered broker-dealer. SMBC Nikko Securities Canada, Ltd. ("SMBC Nikko Canada") is a US and Canadian registered broker-dealer. SMBC Capital Markets, Inc. ("SMBC Capital Markets") is provisionally registered with the CFTC as a US swap dealer. In the US, capital markets and other investment banking activities for SMBC Group are performed by a combination of SMBC Nikko America, SMBC Nikko Canada, and SMBC Capital Markets. Lending and other commercial banking activities are performed by Sumitomo Mitsui Banking Corporation and its banking affiliates. Derivative activities may be performed by SMBC Capital Markets or Sumitomo Mitsui Banking Corporation. SMBC Group deal team members may be employees of any of the foregoing entities.

This document is for informational purposes only and is not intended to be a research report, advice, a recommendation, an offer to sell or the solicitation of an offer to buy any securities, enter into any transaction or adopt any hedging, trading or investment strategy, or any commitment to underwrite, subscribe for, or place any securities, is not an offer or commitment to provide any financing or extension of credit or service, and does not contain any tax or legal advice. Any transactions or strategies discussed herein do not take into account the particular investment objectives, financial situations, or needs of any client, and may not be suitable for all parties. This document is not subject to the independence and disclosure standards applicable to research reports and research analysts under those laws and regulations. This document has been prepared for and is directed exclusively at Qualified Institutional Buyers, sophisticated institutional investors, and other market professionals. It is not intended for distribution to or use by retail customers.

In preparing this document, SMBC Group has relied on information available from third parties, including public sources, and we have assumed, without independent verification, the accuracy and completeness of such information. Specific prices, indices or measures, including ranges, listed in this document were prepared at or around the time the document was prepared, and are subject to change without notice. SMBC Group makes no representations to, and does not warrant, this document's accuracy or completeness. SMBC Group expressly disclaims any liability for any results in connection with use of the information set forth herein, including, without limitation, any use of the information in the preparation of financial statements or accounting material. Prior to participating in any transaction or strategy, you should consult your own independent, competent, legal, tax, accounting and other professional advisors. SMBC Group does not provide tax advice. Accordingly, any discussion of U.S. tax matters contained herein (including any attachments) is not intended or written to be used, and cannot be used, in connection with the promotion, marketing or recommendation by anyone unaffiliated with SMBC Group or for the purpose of avoiding U.S. tax-related penalties.

This document may contain forward looking statements, which may include projections, forecasts, income estimates, yield or return, future performance targets, or similar analysis. Any such forward-looking statements, prices, indices, or measures are based upon certain assumptions. All forward-looking statements are based on the information available at the time the document was prepared and SMBC Group is not obligated to provide an update. Actual events may differ from those assumptions or available information. Any opinions, projections, price/yield information or estimates are subject to change without notice. There can be no assurance that any estimated returns or projections will be realized, that forward-looking statements will materialize, or that actual results will not be materially different from those presented herein. Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. The value, price or income from transactions or strategies may fall as well as rise. SMBC Group or an affiliate may have a position in any of the underlying instruments, assets, indices or rates mentioned in this document.

This document is confidential and is the property of SMBC Group subject to copyright, and is furnished by SMBC Group solely for use by the client or potential client to whom such materials are directly addressed and delivered. Any reproduction of this document, in whole or in part, is prohibited, and you may not release this document to any person, except to your advisors and professionals to assist you in evaluating the document, provided that they are obligated, by law or agreement, to keep the document confidential.