

## Is Helicopter Money Next?

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### Key Points:

- 1 Negative interest rates policies (NIRP) do not appear to have succeeded in pushing up inflation
- 2 Monetary policy debate has shifted back to textbook stimulus via fiscal deficit monetization
- 3 Political risk is becoming an increasingly relevant component of the market outlook

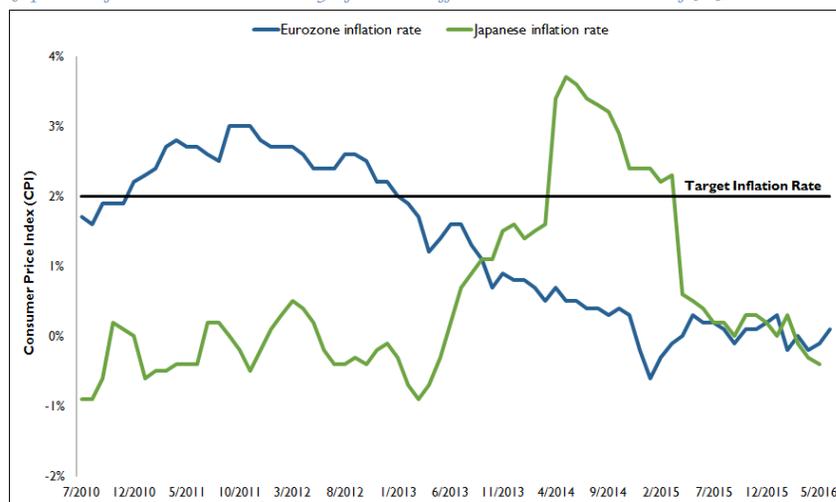
### RIP NIRP?

At the end of the first quarter we were taking stock of the latest monetary experiments implemented by global central banks in the hope of creating economic growth and inflation: central banks in Europe and Japan have taken interest rates into negative territory. While some of the latest economic growth data in Europe and Japan are encouraging, the low cost of capital and negative interest rates do not appear to have succeeded in pushing inflation up towards the central banks' targets or encouraging positive market sentiment.

#### Fig 1: Inflation in Japan and Eurozone below the 2% target

Eurozone inflation rate source: Eurostat as of 6/30/2016.

Japanese inflation rate source: Ministry of Internal Affairs & Communications as of 5/31/2016.



While interest rates in the Eurozone and Japan may not come back to positive territory anytime soon, the policy debate has shifted back to textbook monetary stimulus via fiscal deficit financing/monetization: governments stimulate economic activity via fiscal spending, while central banks print money to finance the spending. This method of stimulating economic activity and inflation is also referred to as “helicopter money.” While helicopter money appears to be the next logical step in the minds of analysts and commentators, it requires coordination between monetary and fiscal authorities, which is presently not a trivial constraint. Meanwhile, we believe central banks’ monetary experiments are more likely to generate market volatility than ease it.

### Looking ahead

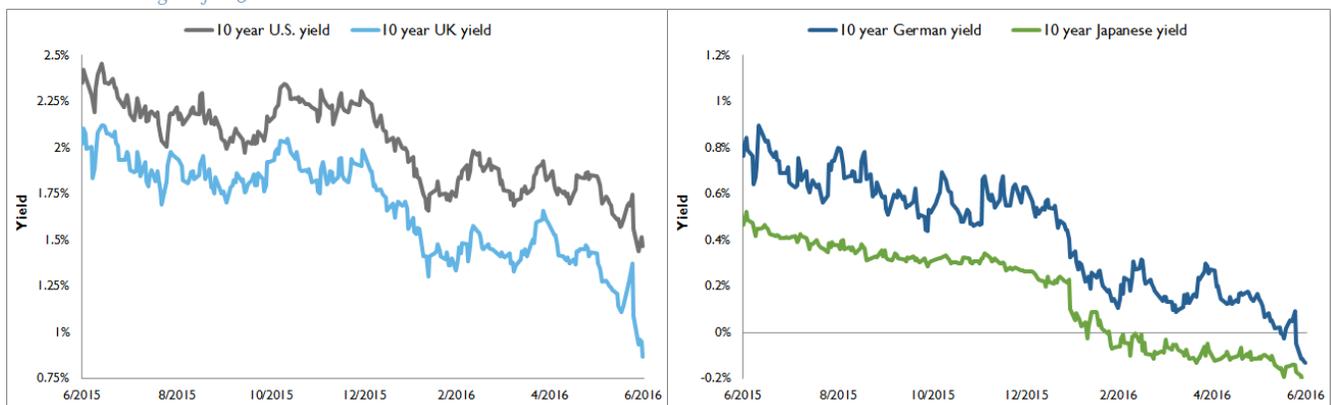
Prospects for global economic growth and inflation remain quite weak. Central banks are likely to continue their interventions in an attempt to boost inflation and economic activity. Weak growth and inflation, together with central banks’ intervention, could continue to result in rather low and in many cases negative global yields.

The U.S. Federal Reserve (Fed) remains front and center when it comes to the market outlook. While the U.S. economic recovery appears intact, the Fed will likely approach interest rate hikes gingerly in light of volatile market sentiment and global economic and market conditions. The theme of monetary policy divergence is still very relevant and as global central banks intervene to ease monetary policy further, the U.S. dollar could strengthen. A stronger dollar would tighten financial conditions and be a reason for caution in proceeding with any further interest rate increases. The Fed will therefore pay attention not just to its monetary policy stance in relation to U.S. economic activity, but it will continue to focus on the actions of global central banks and global market sentiment.

Both domestic political and geopolitical risks are becoming an increasingly relevant component of the global market outlook. The recent referendum on Brexit shook the market not only in the weeks and months ahead of the vote, but will likely remain a source of uncertainty as the exit process unfolds.

**Fig 2: Global yields hitting new lows**

Source: Bloomberg as of 6/30/16



Looking beyond Brexit fever, it appears that the process of political integration in the European Union remains challenged. Major European economies like France and Germany will have elections in 2017, while presidential elections in the United States could become an increasingly relevant market theme ahead of the November 2016 elections and possibly beyond.

China, the second largest economy in the world, continues to juggle the challenge of achieving a 6.5-7% real gross domestic product (GDP)<sup>1</sup> growth target by supporting credit expansion in the economy, while at the same time managing its growing stock of debt. The relevance of China in the global markets and economy will also continue to make it an important driver of global sentiment going forward.

### Windhaven Positioning

Weak growth and inflation, persistent unorthodox global monetary policy measures such as negative

interest rates and geopolitical risk have created an environment of uncertainty and record low yields across much of the developed world. Uncertainty and low yields have pushed investors towards asset classes that are perceived as safe havens such as gold and U.S. treasury bonds, but also towards higher yielding and interest rate sensitive asset classes.

With this backdrop, throughout the past quarter our modeling framework has led us to take a cautious stance on risk across our strategies. We have maintained low exposure to European asset classes where there is little positive momentum, kept moderate exposure to low yielding U.S. fixed income, and have added to our gold and interest rate sensitive asset classes like real estate both of which currently have positive momentum and benefit from low interest rates globally. Our investment process is also finding high-yielding dollar-denominated emerging market debt attractive and we added a position as a result.

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<sup>1</sup>Source: National Bureau of Statistics of China

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The information provided herein is for general informational purposes only and should not be considered an individualized recommendation or personalized investment advice. The strategies mentioned here may not be suitable for everyone. Each investor needs to review an investment strategy for his or her own particular situation before making any investment decision.

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International investments may involve additional risks, which could include differences in financial accounting standards, currency fluctuations, political instability, foreign taxes and regulations, and the potential for illiquid markets. Investing in emerging markets may accentuate these risks. Fixed income securities are subject to increased loss of principal during periods of rising interest rates. Fixed income investments are subject to various other risks including changes in credit quality, market valuations, liquidity, prepayments, early redemption, corporate events, tax ramifications and other factors.

Windhaven's risk management process includes an effort to monitor and manage risk, but should not be confused with and does not imply low risk or the ability to control risk.

Diversification strategies do not ensure a profit and do not protect against losses in declining markets.

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**Please refer to Windhaven's ADV Part 2 for additional information. 7/2016**  
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