



# The run-off of the Fed and ECB balance sheets weighs heavily on the future of the equity markets

## COLLATERAL DAMAGE

There is a certain indicator that, over the last few decades, has always offered a faithful representation of what has been happening on the equity markets: the balance sheets of the main central banks. When the balance sheets are growing, with expansive policies, equity performs well; conversely, when they are shrinking, the stock markets find themselves in trouble. What we've been seeing in the last few months is the same as what happened in 2018 when, after years of QE, we saw the first attempt to halt the rise of balance sheet assets, mainly by the Fed.

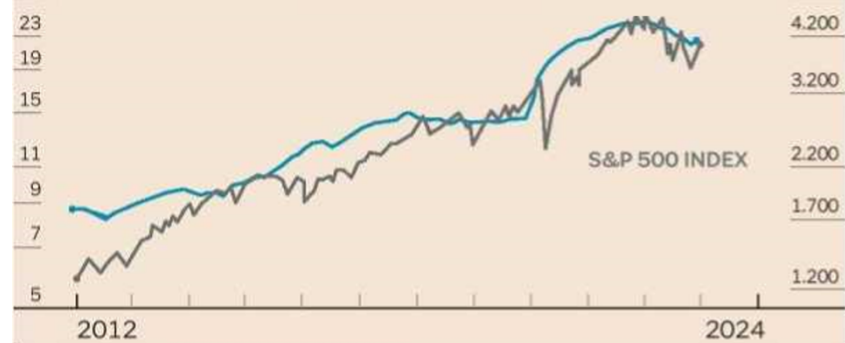
"The growing balance sheets of the central banks is one of the factors that supported the economy during the pandemic and created that spike in inflation that we're currently tackling with the interest rate rises in 2022," explains Angelo Meda, Head of Equities at Banor. "At the moment we're seeing a strong correlation between money creation and the trend of the equity markets across a six-month horizon. The forecast suggests a continued liquidity drain in the coming quarters, both to rebuild margins in case of a recession, and because values are at historical highs. Whatever the conditions, this will have a negative effect on the equity and bond markets, even if in the short-term the most

## Comparison

### The dynamics

TOTAL ASSETS OF THE FED, ECB AND BOJ (LEFT) in trillions of dollars

S&P 500 INDEX (RIGHT) In points



Source: Yardeni

decisive factor in determining market trends will be whether or not we experience a bad recession." The onset of a recession could open the doors to potential new expansive interventions by the central banks, liking bringing relief to the asset classes.

The balance sheet of the Federal Reserve currently stands at 8,300 billion dollars, around a third of US GDP. This is not far off the peak of 9,000 billion reached in April this year. The ECB, however, is still around its peak at approximately 8,500 billion euros. Japan is the exception, where the

central bank's assets represent around 130% of GDP. Tokyo is continuing its ultra-expansive policy and at the moment the main victim of this strategy is the yen, which has plummeted to its lowest level against the US dollar in twenty years at around 150, albeit with some recovery in the last few weeks.

**THE REDUCTION INTERVENTION IS WELL UNDERWAY IN THE US BUT IS YET TO TAKE OFF IN THE EUROZONE**

-An.Gen.