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The Aerial View

Morning Briefing

Then And Now

- **Backdrop to current events carries distant echo of 1987**
- **Trends in 1987 were more mature and more extended**
- **Short term dynamics carry some similarities as well**

Fed chair Alan Greenspan had been in his role for just two months when the stock market crash of 1987 hit. The run up to October 19 coincided with the latter stages of a USD downtrend that had seen the index fall over 40% while the S&P 500 had surged by a further 75%. However, headline inflation had been rising from the start of the year (rising from 1.5% to over 4%) prompting the Fed to raise the discount rate in September (the first hike since 1981).

The immediate lead up to the crash took about nine trading sessions with the lions' share concentrated in the last three trading sessions (with the S&P 500 down about 10%). The USD came under renewed pressure during this period.

The Asian trading session of October 19 proved mild (given what was about to follow) with the TOPIX dropping 2.3%. However, the trend gained ground during the European session with the FTSE 100 dropping about 6% by 9:30 AM (although there was a degree of catch up taking place given the London market had been closed on the previous Friday). By the close of play the S&P 500 was down over 20%, its largest ever daily decline.

Simon Derrick
Chief Currency Strategist,
BNY Mellon

Email >

Newswatch

1.

Japan: BoJ Governor Kuroda says: "It's inappropriate to prematurely shift monetary policy just to create future policy space". >

2.

Australia: The RBA keeps interest rates at 1.5% >

The immediate lead up to the crash took about nine trading sessions

After precipitous declines during the next Asian session (the TOPIX lost over 14%) and before the opening of US financial markets , the Federal Reserve issued a short statement that said: "The Federal Reserve, consistent with its responsibilities as the Nation's central bank, affirmed today its readiness to serve as a source of liquidity to support the economic and financial system." Whether or not this was the catalyst behind the market's subsequent recovery (alongside the Fed’s use of open market operations to drive interest rates down by more than 50 bp on the day to below 7%), this marked the start of an era during which investors came to believe in the power of central banks to manage severe market downturns.

So how does today compare to 1987? The first thing to note is that the USD has been trending lower for a significantly shorter period (just 13 months) and that the decline to date stands at around 13.5%. Equally, the rally seen in the S&P 500 over the same period (as of the end of last month) stood at a more modest 25%.

The current decline began six sessions ago

Turning to the shorter term dynamics, it’s worth noting that the current decline began six sessions ago and has so far seen a drop of 7.7% (with the lion’s share of the move coming over the past two trading sessions - 5.6%). As far as today’s Asian trading session is concerned, the losses have echoed those seen in the US yesterday with the TOPIX currently down 4.4%, the Straits Times Index just over 3% and the Hang Seng Index a substantial 5.3%.

How the new chair of the FOMC responds should the situation continue to deteriorate will be key not just to the immediate outlook but to understand whether the Fed put still exists.
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3.

Australia: Retail sales fell by 0.5% m/m in December following growth of 1.2% in November >

4.

Euro-zone: The CDU and SPD have agreed to continue negotiations for a further day to secure a Grand Coalition >

5.

Euro-zone: German industrial orders rose by 3.8% m/m in December- far exceeding expectations for a 0.7% increase >

On the Radar

February 6, 2018

• US Dec international trade (1330 GMT): Reuters consensus forecast - USD 52 bn; previous - USD 50.5 bn

• CA Dec trade balance (1330 GMT): Reuters consensus forecast - CAD 2.2 bn; previous - CAD 2.54 bn

AerialView@BNYMellon.com

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The Bank of New York Mellon 225 Liberty Street, New York, NY 10286

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