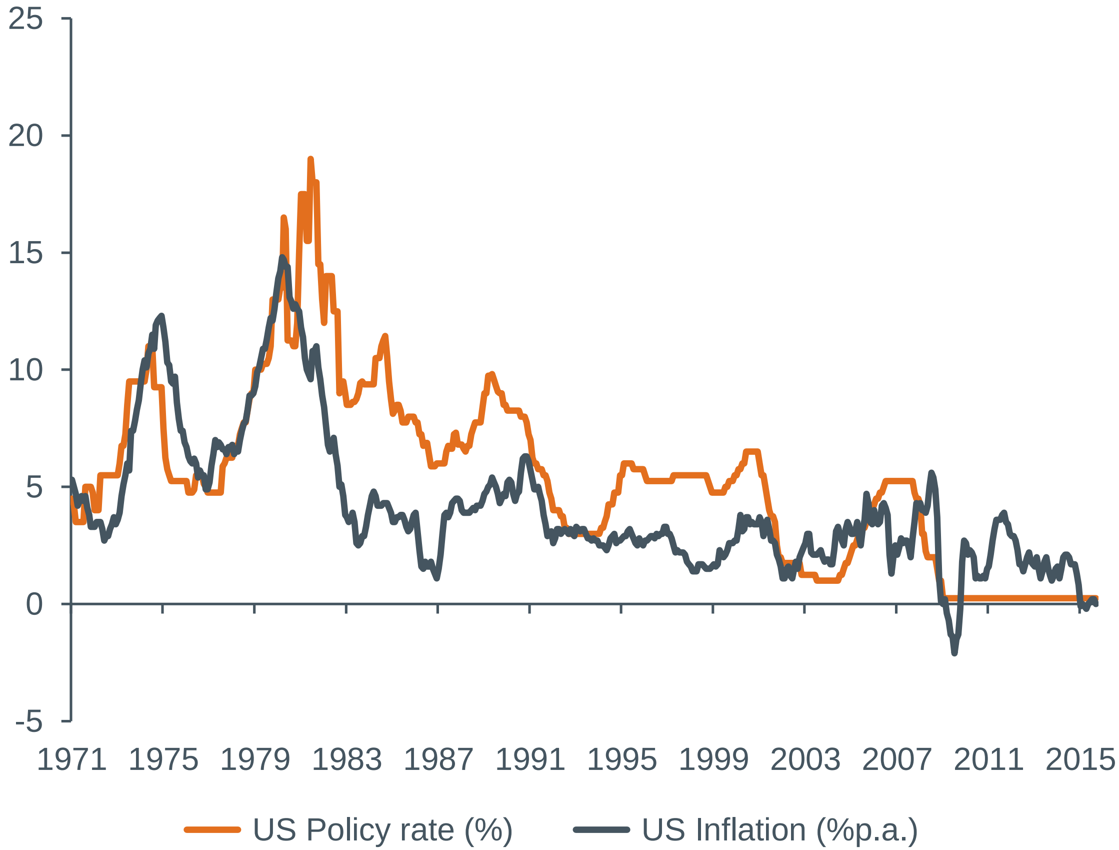
Monetary policy
Trends and consequences

November 2015

Scott M Jamieson – Head of Multi-Asset Investing

Whatever it took



- **In 1979 Paul Volcker (president of the US Federal Reserve) resolved to deal with inflation**
  - Whatever it took
- **He maintained a positive real policy interest rate of 4% for more than a decade**
  - To get inflation down to around 5%
- **Then at 3% for another 8 years**
- **To get inflation to 2-3%**
- **No one thought that originally it would require so much**

With inflation still heading downward and now at zero, what is needed to take it higher?

Source: Datastream and Bloomberg as at September 2015

Making sure deflation doesn't happen

In 2002 Ben Bernanke (later Chair of the US Federal Reserve) set out what was required to ensure that deflation is avoided. The steps necessary were:

First "the best way to get out of trouble is not to get into it in the first place", to this end the central bank should:

1. Maintain a positive inflation rate
2. Maintain financial stability within the broad economy
3. If action is required, be bold

If deflation is still a threat then:

4. Take the policy rate to zero
5. Set a ceiling for market interest rates/ yields – not just for government bonds
6. Making open-ended purchases of bonds
7. For the CB to act a s a primary lender not just a lender of last resort

Finally if all else fails:

8. Debase the currency

Bernanke never envisaged that even this might not work

Whatever it takes

“the ECB is ready to do whatever it takes ....believe me, it will be enough”

Mario Draghi, President of the ECB, 2012

“What if ‘whatever it takes’ is not enough”

Albert Edwards, Chief Strategist at SocGen, 2015

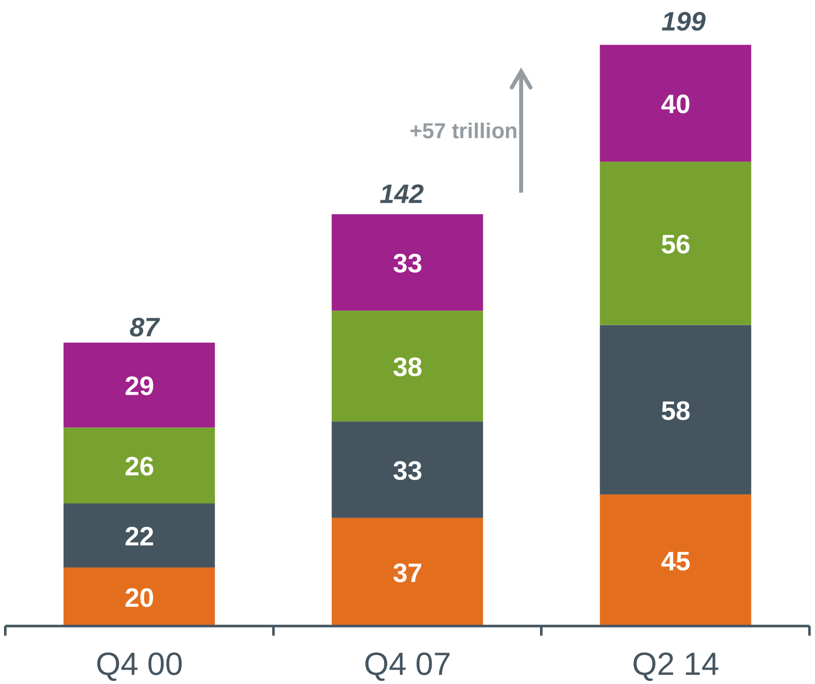
“We have spent several years watching the price of assets going up when there is no reason to suppose that they have got more valuable”

Jonathan Ruffer, Oct 2015

Debt is still growing

KAMES CAPITAL

Global stock of debt outstanding by type, $ trillion, constant 2013 exchange data



Compound annual growth rate (%)	2000-2007	2007-2014
	7.3	**5.3**
Household	8.5	5.3
Corporate	5.7	5.9
Government	5.8	9.3
Financial	9.4	2.9

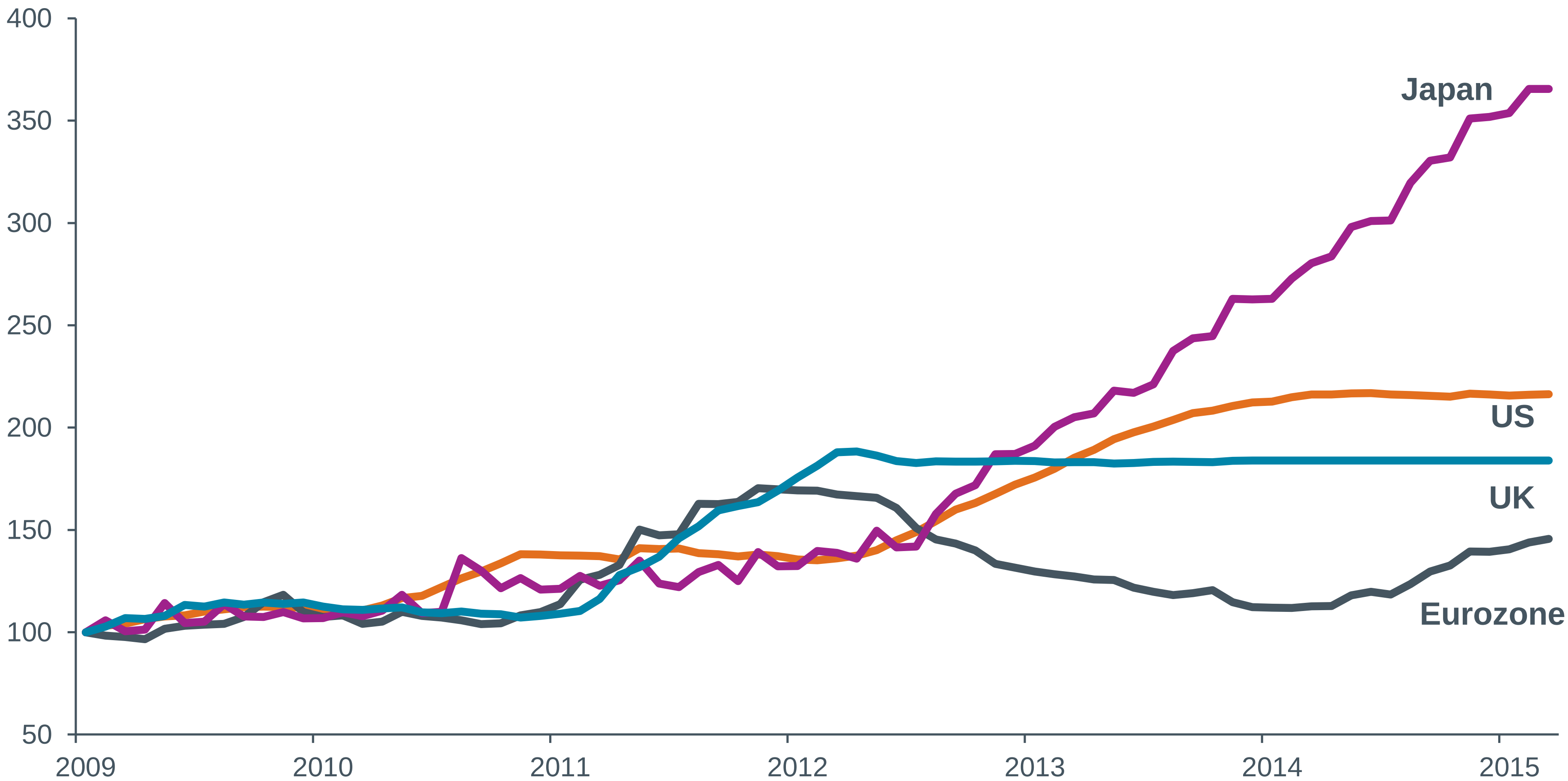
246 ***269*** ***286*** ***Total debt as % of GDP***

Source: Ruffer. For illustrative purposes

Central bank balance sheets ballooned

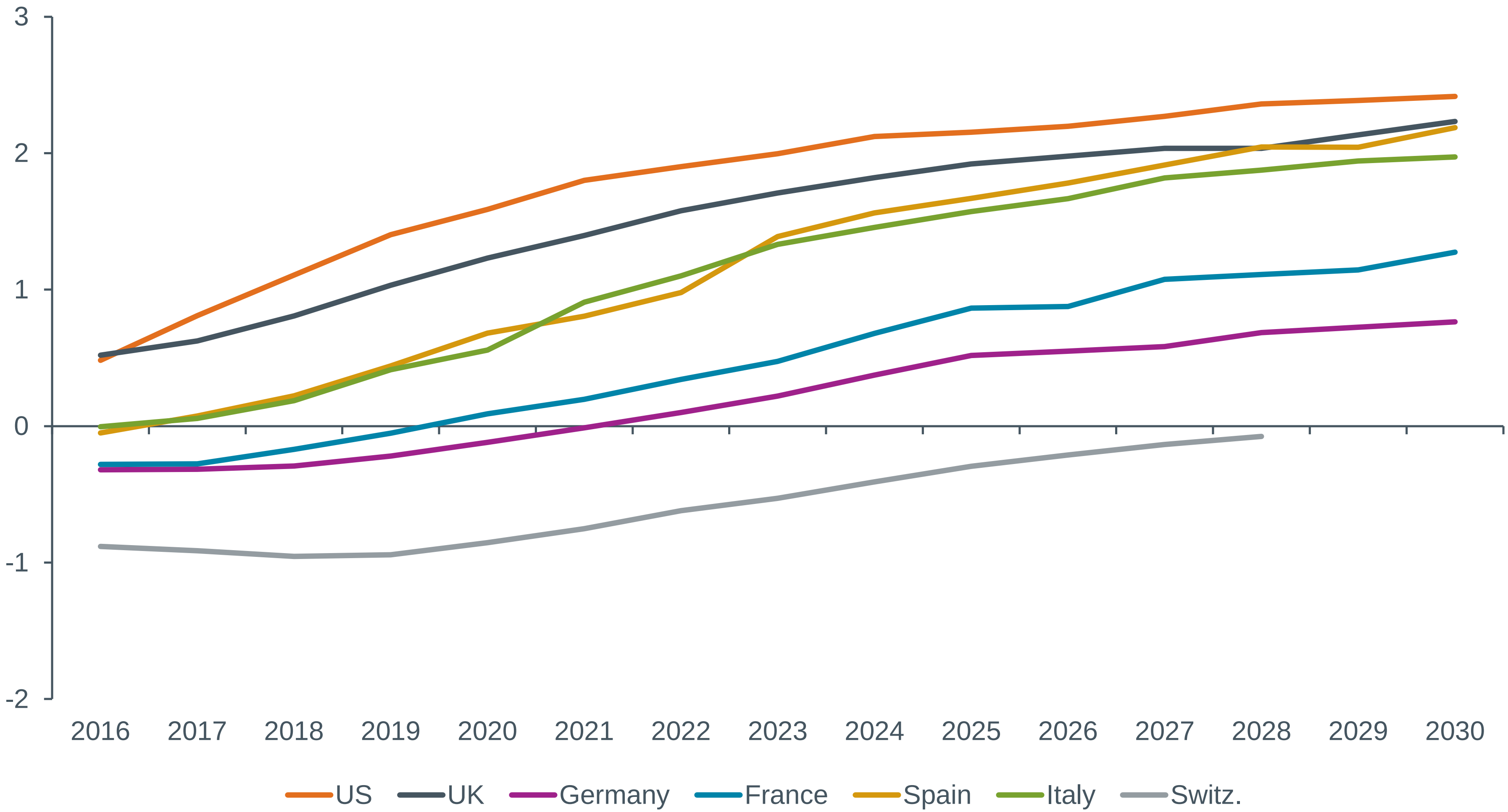
KAMES CAPITAL

Central bank balance sheets



Source: Bloomberg as at October 2015

International bond curves (%)

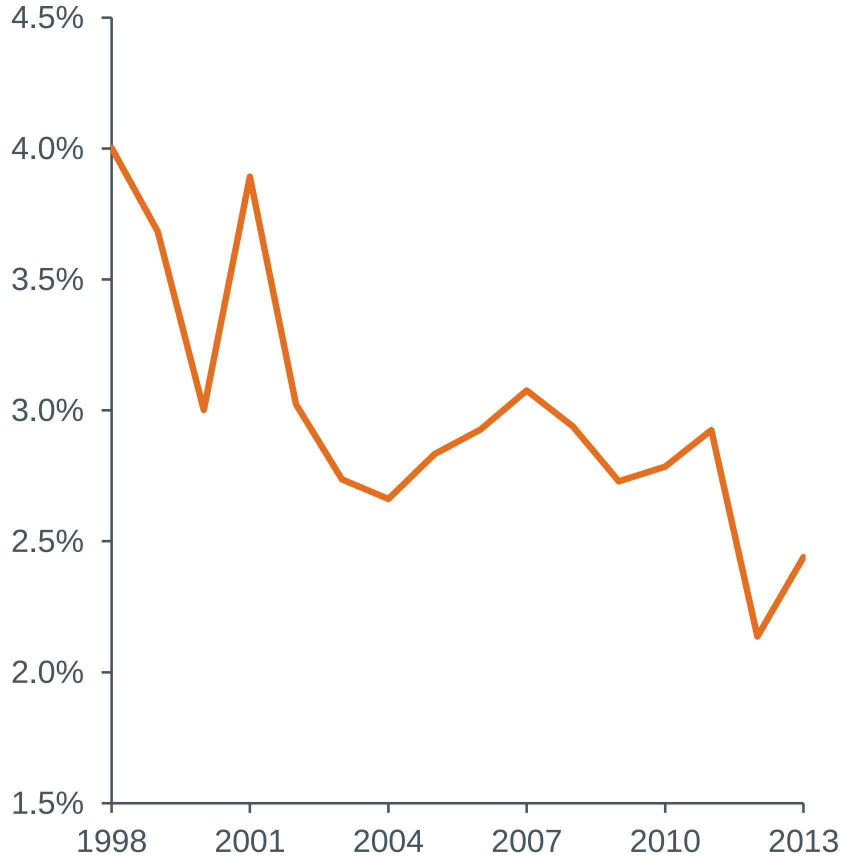


Source: Bloomberg as at October 2015

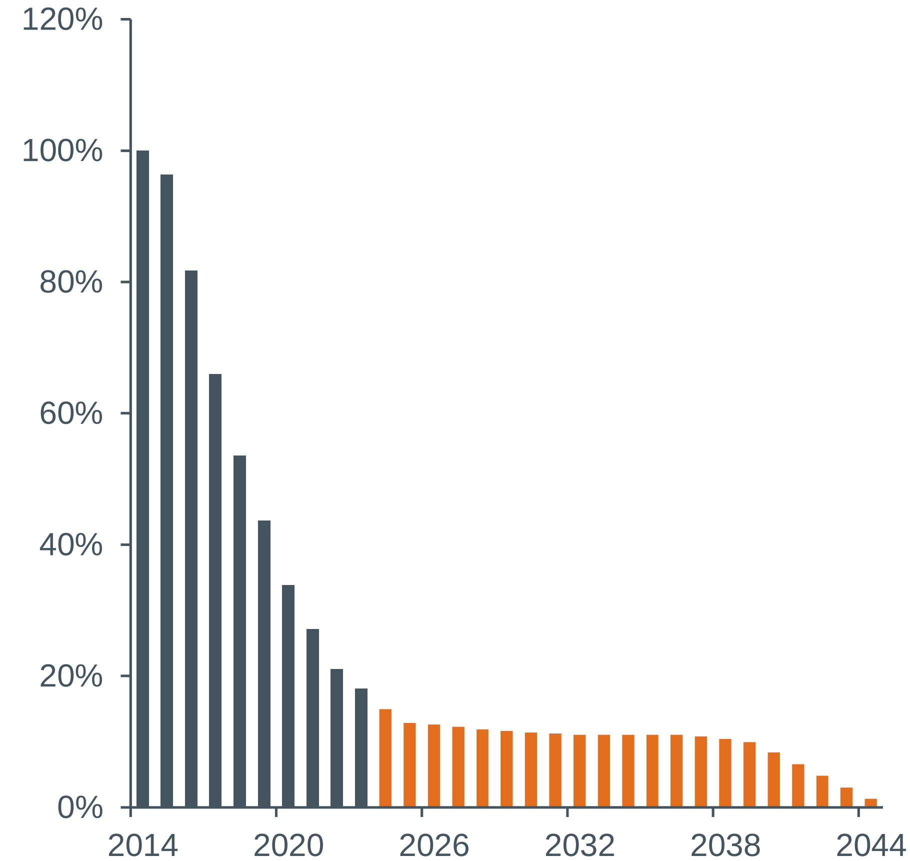
But borrowing costs have fallen?

KAMES CAPITAL

US debt repayments as % of GDP



US Maturity Chart



Average coupon on new debt in 2013 was 1.3%

Source: Datastream as at 31 December 2013

Important information

KAMES CAPITAL

This document is not intended for retail distribution and is directed only at investment professionals. It should not be distributed to, or relied upon by, private investors.

All data in this presentation is sourced to Kames Capital unless otherwise stated.

The views expressed in this document represent our understanding of the current and historical positions of the market. They should not be interpreted as a recommendation or advice.

"This document is accurate at the time of writing but can be subject to change without notification. Kames Capital is an Aegon Asset Management company and includes Kames Capital plc (Company Number SC113505) and Kames Capital Management Limited (Company Number SC212159). Both are registered in Scotland and have their registered office at Kames House, 3 Lochside Crescent, Edinburgh, EH12 9SA. Kames Capital plc is authorised and regulated by the Financial Conduct Authority (FCA reference no: 144267). Kames Capital plc provides segregated and retail funds and is the Authorised Corporate Director of Kames Capital ICVC, an Open Ended Investment Company. Kames Capital Management Limited is an appointed representative of Scottish Equitable plc (Company Number SC144517), an Aegon company, whose registered office is 1 Lochside Crescent, Edinburgh Park, Edinburgh, EH12 9SE (PRA/FCA reference no: 165548)."