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Trump Back on Track; More Fed Vacancies

Friday, 5:50 p.m. EST

Markets continue to react to Trump's actions. When he met on Thursday with the airline CEOs and spoke of lower taxes, less regulation and better infrastructure, the equity markets surged, and gains continued today with all four major averages (S&P, Dow, Nasdaq, and Russell 2k) all hitting all-time highs. On the whole business and economists do not like Trump's immigrant ban and all the controversy earlier in the week weighted on the market. The Appeal Court's unanimous decision to oppose the president's ban sets the stage for a legal struggle, which may be protracted.

On Wednesday the yield on the ten year Treasury sank to 2.34%, 26 bps below the high reached on December 14 after the Trump election. Most of the buying came from Europe as the 10-year German bund yields sank 20 bps to 0.29% before recovering. The flight to the bund Germany is motivated by the fear that the surge of right wing parties raises the probability that the Euro and/or the EU will break apart.

I am on record saying that I believe that the breakup of the Euro is an extremely low probability event. Europeans do not want to exchange their hard Euros for a much softer national currency. Many French have memories of the franc depreciating 100 fold in the early 1950s and the Italians have even worse memories of the lira. The Greeks would have gained significantly by dropping the Euro, but they refused to give up their Europe and Prime Minister Tsipras had no choice but to capitulate to German demands. As fears of a Euro breakup ease, many of the risk-on markets should recover in Europe.

Today it was announced that Daniel Turullo, a member of the Federal Reserve's Board of Governors who spearheaded financial reforms and regulations that followed the financial crisis, announced his resignation in April, as had been expected. That means there will be soon be 3 opening on the 7-member Board and bring the voting strength of the Board below that of the regional bank presidents. In addition, Trump had announced he will replace Janet Yellen and likely Stanley Fischer when their terms expire next year. That would mean Trump could soon appoint 5 of the 7 members of the Fed's Board, an unprecedented event. (Board members have staggered 14-year terms; Yellen and Fischer could remain on the Board after being stripped of their chairmanships, but such outcomes are extremely rare.) These appointments could be the most important policy appointments Donald Trump makes.

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