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The Tide Beneath the Markets: Understanding Global Liquidity

Richard Harris | August 2026

Markets rarely move for the reasons the headlines suggest. A company can report excellent earnings yet watch its share price fall. A country can lurch from crisis to crisis while its market climbs to record highs. Something less visible is often at work: liquidity, perhaps the most powerful force in global finance, and one few people have had explained to them.

We saw it in action this month. The US Treasury surprised markets by announcing it would double its buybacks of long-term government bonds, stepping in as an extra buyer to calm a market where 30-year borrowing costs had just hit a 19-year high. No earnings, no economic data, just a shift in who was buying. That is liquidity at work, and why we thought it would be a good topic to dig into in this month's newsletter.

What Do We Actually Mean by “Liquidity”?

At its simplest, liquidity is how much money is moving through the financial system and how easily it flows. Two ideas are often confused: the price of money (the interest rate, or what it costs to borrow), and the quantity of money, how much cash and credit is available to be lent, spent and invested. Interest rates grab the headlines, but quantity is just as important, and where the real story often lies.

When liquidity is plentiful, money is easy to come by: investors feel confident, credit flows freely, and most assets rise. When it drains away, the opposite happens: funding turns scarce, lenders grow cautious, and prices come under pressure. Think of it as the tide. When the water rises, most boats rise with it, and when it goes out, the rocks appear.

Where Liquidity Comes From

There are two major sources of liquidity. The first is government, through fiscal policy. When a government spends more than it collects in tax, it puts money directly into the economy through salaries, grants, infrastructure and payments to citizens, funding this by borrowing. It can also adjust the flow through tax (cut taxes and households keep more; raise them and liquidity is withdrawn).

The second is the central bank, through monetary policy. Central banks set short-term interest rates, but they wield a more powerful, less understood tool, their own balance sheet. By creating money to buy bonds (quantitative easing, or QE), they inject liquidity into the system. By letting those bonds mature (quantitative tightening, or QT), they drain it out again. This is money creation and destruction on an enormous scale, largely out of public view.

When the Alarm Bells Ring

It is in a crisis that these forces show their true power. During the 2008 financial crisis, and again in the 2020 pandemic, governments and central banks acted together at extraordinary speed: rates were slashed, trillions created to buy bonds, and money sent directly to households and businesses, “whatever it takes.” The effect can be striking. In 2020, equity markets worldwide rebounded to record highs within months, even as the real economy suffered the deepest recession since the Great Depression, a vivid reminder that markets and the economy are not the same thing, and that liquidity is often what separates them.

We have made this point before and will make it again: when the system is under real stress, policymakers will do whatever it takes to keep it functioning. This tendency, to flood the system with liquidity in bad times and to be slow to withdraw it in good times, has been a persistent tailwind for financial assets over the long run.

Who Controls Global Liquidity?

Global liquidity is not controlled by any single institution, but four central banks dominate it. The US Federal Reserve is by far the most important, because so much of the world's trade, debt and savings is denominated in dollars. That makes the Fed the tide-setter for everyone: when it makes dollars scarcer,

ripple through every market on earth, including our own.

How Global Debt shapes liquidity

The four regions mentioned above share one further trait: all carry heavy government debt, usually gauged against gross domestic product, or GDP (the value of everything an economy produces in a year). Japan's is the developed world's heaviest, above 200% of GDP. The United States sits near 125%, and Italy, France and others exceed 100%. China's headline figure is lower, near 85%, though much borrowing sits with its local governments. Debt on this scale bears on liquidity two ways. Governments must keep borrowing just to repay maturing loans, continually drawing cash from the system, and heavy debt makes it hard to hold rates high for long, as servicing costs rise too. The result is a lasting pull towards keeping money plentiful and cheap, a steady tailwind for markets. But investors are beginning to note the perhaps unsustainable level of global debt, and starting to demand higher returns for the risks attached.

The picture varies by region, but the direction is the same. In the United States, the government spends far more than it collects, and interest on its debt now costs more than the entire defence budget, a powerful reason to favour lower rates. Japan has gone furthest: its central bank owns more than half the government's bonds. Among the euro countries, one central bank must keep conditions loose enough for its most indebted members, such as Italy and France, to keep borrowing. In China, the authorities lean on state banks to keep credit flowing whenever growth slows. In each case, the weight of debt tilts policy towards adding money rather than withdrawing it.

How Liquidity Moves Markets

When liquidity is added, it does not sit still but searches for a return. It usually flows first into the assets most sensitive to easy money: shares, especially fast-growing technology companies, and the more speculative corners of the market. Property and corporate bonds usually benefit too, and emerging markets, ours included, often attract these flows as investors reach further afield for higher returns. Because rising asset prices reward those who already own assets, abundant liquidity tends to benefit the wealthy most, widening the gap between those with capital and those without.

When liquidity is drained, the process runs in reverse, and usually faster. The most speculative assets fall hardest, investors retreat to safety, and borrowing costs rise for everyone. Government bonds and, at times, gold have historically served as safer harbours, though no asset behaves the same way every cycle. There is a subtler lesson too: when liquidity drives everything, assets that normally behave differently can rise and fall together, so the shelter diversification offers may shrink just when it is most needed. It is one reason we spread our clients' capital across many holdings, asset classes and regions. This does not let anyone predict markets, but it explains much of what we observe.

Where the Tide Stands Today

The current picture is fascinating, because the world's most important central bank appears to be pulling two levers in opposite directions. On the one hand, the Fed (now under a new chair, Kevin Warsh) has held interest rates high, in a range of 3.5% to 3.75% for the fifth consecutive meeting, as it wrestles with inflation that has stayed above target for years. On this measure, money remains relatively expensive.

On the other hand, and far more quietly, the Fed stopped shrinking its balance sheet at the end of 2025 and has since made modest monthly bond purchases to keep the banking system well supplied with cash and more recently the US Treasury increased buying on longer dated US bonds to try keep rates lower (some may call this yield curve control). Meanwhile, the broad US money supply has climbed to a record above US\$23 trillion, and China has reached fresh highs of its own. The European Central Bank and the Bank of Japan have gradually allowed liquidity to ebb.

How worried you should be depends on how you measure liquidity. Measured narrowly, by the money supply, conditions are still loosening. A wider lens looks past the money stock to the plumbing of global funding markets and the shape of the bond market. On that view, a shrinking gap between short- and long-term rates signals liquidity draining away. By these faster measures, it peaked around February and has been tightening ever since, in line with a firmer Fed — and because such shifts take many months to bite, the worst may still lie ahead. The main offset is China, which has recently opened its monetary taps again. No single gauge has a monopoly on the truth.

The result is a more balanced and selective environment than the flood of recent years, neither the open tap of the pandemic nor a genuine drought. The quiet return of money creation, even as its price stays high, is well worth watching.

To Conclude

Liquidity operates beneath the surface of markets. It offers no forecast of the weeks ahead, but it accounts for much of how markets behave, and it underpins our commitment to diversification, patience and discipline. We hold a broad spread of assets and geographies precisely because the timing of such shifts cannot be known in advance. Our responsibility is to ensure that our clients remain resilient through them.

Market Update

US markets recovered strongly in August, reversing much of July's technology sell-off. The Nasdaq 100 led the way, up 4.10%, followed by the S&P 500 at 2.62% and the Dow Jones at 1.34%. Smaller companies lagged, with the Russell 2000 gaining 0.86%. The turnaround was driven largely by softer

rate increase and eased a key pressure on share prices. Sentiment also improved mid-month when the US Treasury announced it would at least double its buybacks of longer-dated government bonds, which investors read as supportive for markets. However, the tone turned more cautious late in the month after Federal Reserve Chairman Kevin Warsh voiced concern about inflation at the Jackson Hole symposium, lifting the perceived odds of a rate increase. The dollar weakened 0.5%, while the 10-year government bond yield was little changed, edging up from 4.740% to 4.756%.

European markets were mixed. Germany's DAX rose 2.45% and the broader Stoxx Europe 600 gained 0.98%, supported by the improving global backdrop. France's CAC 40 fell 2.06% and the UK's FTSE 100 slipped 0.40%, the latter held back despite firm commodity prices. The unresolved standoff over the Strait of Hormuz remained a drag on sentiment, with the US blockade still in force and negotiations with Iran deadlocked, keeping oil prices elevated and inflation risks in focus for the region's energy-importing economies.

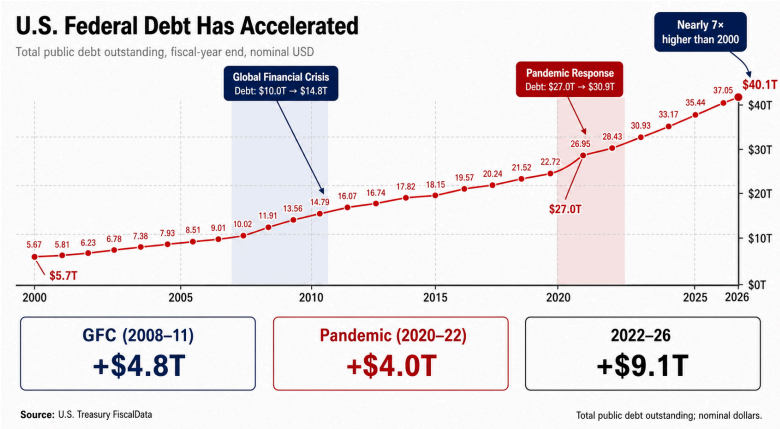
In Asia, China's Shanghai Composite was the standout, rising 4.02% as banking and resource stocks rallied and the government announced fresh measures to support the struggling property market. This came despite economic activity data remaining soft, with business survey readings still pointing to mild contraction. Japan's Nikkei 225 gained 3.03%, helped by a weaker yen, which flatters the earnings of Japanese exporters, although Japanese government bond yields rose from 2.799% to 2.947% as expectations built that the Bank of Japan may tighten policy further. Hong Kong's Hang Seng eased 1.23%, giving back a small portion of July's exceptional 13% gain.

Precious metals were the story of the month. Gold surged 9.93% and silver jumped 15.37%, with platinum up 8.45%. The rally was driven by cooler US inflation data reducing the prospect of higher interest rates, which lowers the opportunity cost of holding gold, and was given a further boost by the Treasury's bond buyback announcement, which revived concerns about government debt levels and the dollar. Oil rose more modestly, with Brent up 2.86% and WTI up 1.52%, as the continued closure of the Strait of Hormuz kept supply concerns alive.

Locally, the JSE had an exceptional month, with the All Share Index up 4.31% and the Top 40 gaining 5.33%, both driven almost entirely by the surge in precious metal prices. The Basic Materials sector rose 24.26% as mining shares rallied hard; AngloGold Ashanti, Pan African Resources and Gold Fields each climbed by just over 40%. The rest of the market did not share in the gains. The Technology sector fell 8.43%, weighed down by Naspers and Prosus, which declined despite reporting strong full-year earnings, as investors remained concerned about Tencent's heavy spending on artificial intelligence. The Financials sector slipped 1.58%. The rand strengthened 2.71% against a weaker dollar, supported by the higher gold price and improved appetite for emerging market assets, while the 10-year government bond yield was broadly unchanged, edging up from 8.74% to 8.75%.

Chart of the Month

U.S. federal debt has risen from roughly \$5.7 trillion in 2000 to about \$40 trillion by 2026, underscoring how successive shocks have reset the debt trajectory upward. The global financial crisis lifted debt from approximately \$10.0 trillion in 2008 to \$14.8 trillion by 2011, while the pandemic-era response drove a further step-change, from about \$27.0 trillion in 2020 to \$30.9 trillion in 2022. Since then, borrowing has continued to compound at a rapid pace, leaving the debt stock nearly seven times its level at the start of the century.



“The essence of investment management is the management of risks, not the management of returns.” — Benjamin Graham

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