Shobhana edit

Global central banks try and fill in the breach

While the Fed may not have rolled out a full-fledged QE III when it last met in June but merely expanded Operation Twist by $267 billion, central bankers are quickly adopting a more accommodative stance in their desperation to revive growth and bring down unemployment. On Thursday the Bank of England opted to inject another 50 billion pounds into the economy even as the ECB lowered its main refinancing rate by 25 basis points to a record 0.75% and China cut interest rates for the second time in a month. Even before that the People's Bank of China had been signalling broader monetary easing, ramping up the use of reverse repos in a bid to drive down the cost of short-term money—the bank injected $22.5 billion on July 3, the biggest operation in the last six months. The urgency to flood the money markets stems from the renewed rise in downside risks to global growth. The question, however, is whether these seemingly co-ordinated moves will be enough.

IMF chief Christine Lagarde is on record saying the next IMF growth update, 10 days from now, will see lowered growth estimates. A few days ago, the IMF said US growth in 2013 could halve to 1% if policymakers didn't arrive at an agreement to hike expenditure—no agreement would mean a cut in government expenditure by 4% of GDP, a 'fiscal cliff' the IMF says will lead to 'stall-speed' growth. In Europe, similarly, the ECB rate cut may be of some help but, as we've seen after each major policy step—like the 100-billion euro package for Spanish banks—bond yields crawl back up to unsustainable levels. The big move from the miracle summit last week, of the ECB buying bank bonds directly, can't happen till there is a single banking supervisor, and that's still far away. European PMI is at a 3-year low and, at 45.1, remains firmly in contractionary mode. In China, the impact of the frozen real estate market is yet to work its way through the economy and, with US in decline, the export-push is no longer available—China's PMI fell for the eighth consecutive month in June, to its lowest level since the first quarter of 2009. Not surprising then, most global markets ended in the red despite the central bank actions.

In India, similarly, while an RBI rate cut—our columnist Surjit Bhalla estimates a 100 bps cut results in a 0.44 ppt hike in GDP growth—will help, there is no substitute for policy action by the government. A power plant isn't going to come up, no matter how much you cut interest rates, till the coal mess is sorted out and SEBs become viable; in telecom, similarly, lower interest rates can't work if the government insists on driving up auction prices and keeps the industry in limbo by its Presidential Reference that asks the Supreme Court if another 81 licences need to be cancelled.