International Business News

India's central bank cuts key rate

AFP, New Delhi

India's central bank cut its key short-term lending rate Saturday and announced other monetary steps to spur economic growth as it moved to counter the impact of the global financial crisis.

The Reserve Bank of India, citing "unsettled" financial conditions, reduced its key short-term lending rate, the repo, by 50 basis points to ease a credit crunch and inject liquidity into financial markets. The repo is the rate at which it lends funds to commercial banks.

The bank also announced on its web site it was cutting the amount of cash commercial banks must hold in reserve, easing the so-called cash reserve ratio to 6.5 percent from 5.5 percent -- pumping billions of dollars into the financial system.

And it said it was cutting the statutory reserve ratio -- the proportion of deposits banks must hold in government securities -- to 24 percent from 25 percent to boost liquidity.

Banks around the world have been cutting rates to spur growth, with the US Federal Reserve on Wednesday slashing its main policy rate to one percent and neighbouring China also lowering key interest rates.

Barclays looks to Middle East for cash boost

AFP, London

British bank Barclays said Friday it sought 11.7 billion dollars (9.3 billion euros), mostly from oil-rich investors in Abu Dhabi and Qatar, to bolster its finances amid the global credit crunch.

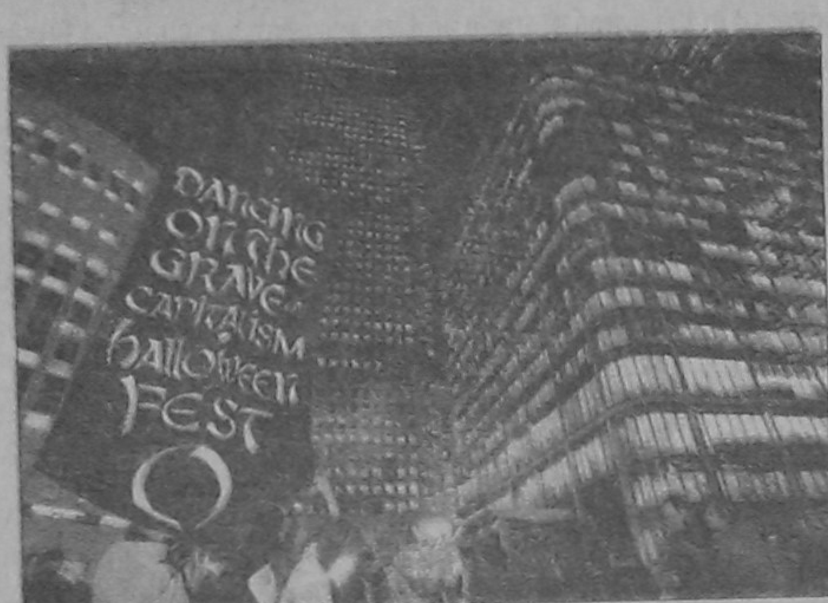
Although the cash call fell slightly short of target, the fresh capital means Barclays will not have to tap funding from the government, unlike some of its competitors, as it grapples with the worst financial crisis in decades.

"The board of directors of Barclays today announces a proposal to raise up to 7.3 billion pounds of additional capital from existing and new strategic and institutional investors," the bank said in a statement.

The cash injection would see Abu Dhabi's Sheikh Mansour Bin Zayed Al Nahyan, a new investor and the owner of English Premier League football club Manchester City, owning as much as 16.3 percent of Barclays.

The Gulf state of Qatar, meanwhile, could ramp up its stake to 15.5 percent from the current level of 8.1 percent.

The announcement ensures that Barclays meets higher capital adequacy targets which were set by Britain's Financial Services Authority earlier this month.



AFP

Anti-capitalist protesters demonstrate outside London's Canary Wharf financial district on Friday. British business minister Peter Mandelson cleared a proposed merger between rival banks Lloyds TSB and HBOS, which had been questioned amid the financial crisis, his office said. Lloyds TSB agreed to buy HBOS in September, as the lender faced collapse owing to massive write-downs caused by the US subprime mortgage crisis and resulting credit crunch.

US consumer spending pulls back 0.3pc in September

AFP, Washington

American consumers cut spending by a sharp 0.3 percent in September in the face of an intense financial market storm, government data showed Friday.

A Commerce Department report said the drop in spending -- which accounts for two-thirds of US economic activity -- came even as incomes rose 0.2 percent.

The decline in spending was the steepest since June 2004, according to officials, and sharper than the average 0.2 percent decline expected by private economists. Adjusted for inflation, the drop was a steeper 0.4 percent.

The September personal income estimate reflects the effects of Hurricane Ike, which struck the Gulf Coast region, causing losses in rental income and property damage, the department noted.

Incomes however grew a bit more than the consensus forecast of a 0.1 percent rise, but inflation-adjusted incomes were up just 0.1 percent.

Intel warns economic crisis may hurt business

AFP, New York

Intel Corp warned on Friday that the economic slowdown may hurt its business but the world's biggest computer chipmaker maintained its fourth-quarter revenue projections.

"The recent financial crisis could negatively affect our business, results of operations, and financial condition," Intel said in a regulatory filing with the Securities and Exchange Commission (SEC).

"Current uncertainty in global economic conditions poses a risk to the overall economy as consumers and businesses may defer purchases in response to tighter credit and negative financial news, which could negatively affect product demand and other related matters," the California group said.

FINANCIAL CRISIS

Twist of fate

SUPACHAI PANITCHPAKDI

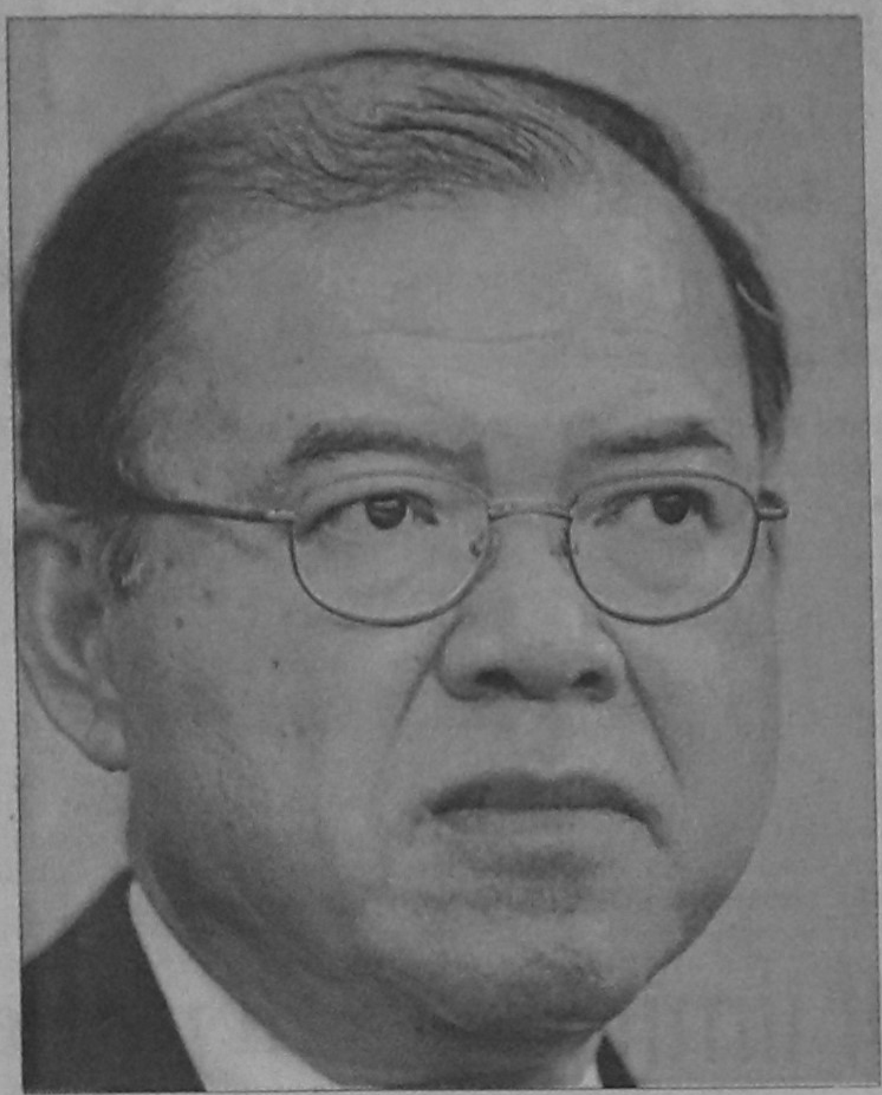
The world economy is being shaken to the core. The global financial crisis is threatening to drag the world into protracted recession, and the prospects for growth -- the key to employment and social development -- are deteriorating fast. As is unfortunately often the case, the poorest countries are likely to be among the worst affected.

Taking the long view of the next 15 years in the midst of an evolving crisis of as yet unknown severity should be approached with caution. Nevertheless, I would like to offer some thoughts on what can be done now to allow the world economy -- and most of all the poorest countries -- to achieve sustained growth in the 15 years to come.

It is a "twist of fate" that the current crisis follows one of the most successful periods of growth the world economy has ever experienced. Between 2002 and 2007, that broad-based growth allowed many developing countries to make significant strides and demonstrated how strongly growth can contribute to development. Between 1996 and 2006, developing countries were able to increase their real income by 71 percent, compared to 30 percent in the G-7 countries. Even the least developed countries, which have experienced erratic growth patterns in the past, have been growing at an average annual rate of more than 5 percent since 2000, much faster than in the late 1990s. Only last year, many LDCs, including Bangladesh, even surpassed 6 percent. Much of this was due to rising demand for commodities, but even exporters of labour-intensive manufactures have been buoyed by high export demand. International trade and investment flows have been crucial to spreading this growth. Indeed, developing countries as a group have seen their exports nearly quadruple over the past decade. This environment has allowed the world to make substantial progress towards the MDGs, with 400 million people being lifted out of extreme poverty between 1990 and 2005. While progress has been uneven, the development gains from recent growth are undeniable.

However, if in those years we have seen the beneficial side of global interdependence, with growth spilling over from country to country, we are now facing the negative side of interdependence, where financial irresponsibility in one country can destroy economic prospects in another. Three crises have exposed the weaknesses of the international system. The troubles began with rising oil prices in 2005, which demonstrated just how much economic progress still depended on a limited supply of fossil fuels. In 2007 and 2008, food prices followed, with devastating consequences for the world's poor. However, it was the crash of the US subprime mortgage market, and the ensuing global financial crises, that finally brought worldwide expansion to a halt.

The precise impact of the crisis remains to be seen, but the UN has already revised its growth projections for the world economy downwards, to about 2 percent in 2009, and this may still be optimistic. Even though this crisis originated in some of the world's most advanced markets, it will clearly have a strong impact on the developing world, including the LDCs. The financial meltdown in advanced economies is filtering through to developing countries in several ways. First, the global deleveraging process is increasingly affecting asset classes that have not so far been considered high-risk, and it is exposing more financial institutions to liquidity problems. In addition to the credit crunch, stock market panics are spreading to emerging markets, with associated impacts on exchange rates, balance of payments and foreign debt. Fears of new currency and banking crises in several emerging markets are therefore justified, even though high levels of reserves mean that some of these markets are better prepared than in the past. Second, developing countries will be affected by a global slowdown in demand, which will in turn affect their export earnings. In particular, a fall in commodity and energy prices due to the expected recession is already reducing growth in producing countries, while at the same time alleviating the burden on importers. The slowdown will further affect remittances, which have become a major source of income for countries like Bangladesh. Finally, if past banking crises are any guide, development assistance is likely to decline, as bailout packages and public guarantees are placing heavy demands on advanced-country budgets.



Supachai Panitchpakdi

While the impact on any individual country will therefore depend on the structure of financial liabilities and reserves of the banking sector and its export structure, it is safe to say that developing countries are unlikely to be decoupled from the crisis. The ILO has recently estimated that the financial crisis will raise global unemployment by 20 million in 2009, and push 40 million people into extreme poverty. Together with the global food crisis, the financial crisis thus risks undoing in a matter of weeks all the progress achieved in poverty reduction over the past six years.

What lessons can we draw from this recent experience? How can we create an economic environment that will enable the world economy, and the poorest countries in particular, to achieve sustained growth without repeated, devastating reversals?

First and foremost on everyone's mind, of course, is the need to rein in global finance. The current global crisis, along with many smaller, more regional crises, has demonstrated more forcefully than ever before that the model of deregulated global finance has failed. Contrary to the predictions of mainstream economic theory, free financial markets are not able to judge risk appropriately, and do not allocate credit effectively. Instead, they are prone to herding behaviour, irrational exuberance and the pursuit of strategies that may be rational for the individual but detrimental to the community. The significant systemic risks they carry means they cannot possibly be left unbound. We thus need to rebalance the role of markets and the role of States. Markets work most effectively in the presence of strong States. What does this mean?

The most urgent priority must be to contain the damage, and to ensure that the impending slowdown does not turn into a global depression. We must accordingly focus not only on supporting banks facing liquidity problems and providing government guarantees, so as to restore confidence, but also on pre-empting the effect on the real economy through fiscal expansion and public investment. In addition, we must soften the blow to the currencies of emerging economies through IMF assistance or emergency loans from reserve-rich countries. Here, there is much scope for more coordinated action, based on the shared objective of averting a global depression.

However, we must also address the immediate and glaring lacunae that have made this crisis possible, through improved regulation and oversight. The first priority must be to reassess the role of credit rating agencies, which have not lived up to their task of providing a sound neutral assessment of risk. We must also devise incentives in the financial sector for simpler financial instruments; and address maturity mismatches in non-bank financial institutions; and bring them under the umbrella of regulation.

Supachai Panitchpakdi is the secretary-general of UNCTAD. The article (part-1) is adapted from his recent speech at an international business conference organised by Dhaka Chamber of Commerce and Industry in the capital. The second part comes in our next edition.

It's liquidity that kills banks

STEPHEN GREEN

Some new lessons need to be learnt or perhaps they are old ones. Financial strength is making a welcome comeback. Benchmarks of acceptable leverage and capital ratios are being revised. And regulators will need to address the procyclicality of capital requirements caused by the interaction of fair value accounting and Basel 2 capital adequacy rules.

There will be a renewed focus on liquidity. This crisis has shown that it is liquidity that kills banks, not just a shortage of capital. Regulators and banks themselves need to understand their liquidity vulnerabilities more clearly.

And the market and industry will need to consider whether badly-aligned incentives have contributed to the crisis: both the market incentives which, until recently, encouraged banks to grow fast and gear up, persuading them to take on higher risk than was sustainable; and compensation structures in the industry, which have so often encouraged too much opacity and excessive risk taking.

But underlying all of this is a fundamental trend in the world economy which, in my view, will not be de-railed even by today's crisis and which we need to recognise for what it is.

And that is the rebalancing of the global economy towards Asia, home to over half the world's population, and its implications for the Middle East. In the long-term, it is this shift that will affect financial markets most profoundly.

Asia and the Middle East will continue to outgrow mature markets. Even in the current economic climate, our short-term projections are for slowing but still quite resilient growth: an expected 6.4 per cent this year slowing to 5.7 per cent next. Given that the emerging markets economies are collectively as large as the US economy, continued growth should help exporters from the G7 countries. But crucially this growth will also stimulate regional and domestic demand for capital.

As Asian and Middle Eastern economies grow larger, we will see the continued development of regional and domestic capital markets. In the light of this financial crisis it would be hardly surprising if caution and scepticism about the Western model of capital markets were to increase amongst emerging markets. Nevertheless, I believe the direction is clear -- regional capital markets will develop and more of the capital generated in the fast growing emerging markets will stay closer to home in the future.

What are the implications of these profound shifts for mature economies over the longer-term? I am not a doomsayer. It is important to remember that economic growth is not a zero-sum game. Therefore the rapid growth of emerging markets does not signal an absolute decline in the economies of mature nations.

The pie will grow. But it does entail a loss of share -- the developed world will have a smaller share of a larger pie. Indeed, this has been the experience of the US since the 1950s.

Capital markets in the developed world will likewise suffer a loss of share. And in the near-term, at least, an absolute decline is also likely as the deleveraging of the financial system works its way through.

And what are the implications of all this for the fast growing regions of Asia and the Middle East?

First, that creating financial systems which are both more sophisticated and more stable will be a major challenge, but it is not one that can be avoided. As economies become larger and more sophisticated, they need fully functioning capital markets to ensure the efficient allocation of capital.

AFP

People shop at a department store in New York City on Friday. The US economy shrank 0.3 percent in the third quarter. The decline was due in part to consumers cutting spending by the largest amount in 28 years, a strong signal that the country has fallen into recession.

For all that the western markets are in crisis, neither the world at large nor Asia in particular can turn the clock back to a simpler era in which capital markets played only a marginal role in economic development.

The main challenge lies in the dichotomy that financial markets, as this crisis has demonstrated, are increasingly global, while the policymakers and regulation that governs them remain predominantly national. Greater international cooperation will be required to place the financial system on a more stable footing. And given that financial crises are a recurrent feature in our lives, we will need more global regulatory coordination to deal with them when they do arise.

At the same time, as Asian and Middle Eastern economies grow and become more important as investors in the world economy, their responsibilities will also become more complex. And their voices will need to be heard in the dialogue about world trade and investment policy that must surely continue.

For there is a clear threat that the financial crisis may rekindle protectionist tendencies. In this new, and more fragile world order, preserving the free-trade and open investment orientation that has helped humanity to become more prosperous than ever before in the last 50 years will be a major challenge, especially if the world faces a major slow-down.

Globalisation is not a new phenomenon; it allowed the world to prosper in the late 19th century when, despite high tariffs, rapidly falling transport costs prompted an explosion in world trade. This earlier wave of globalisation was brought to a halt by the first world war, and then regressed through the 1930s, as a result of protectionist and competitive devaluation with eventually unspeakable consequences.

Since the 1950s, there has been steady progress in liberalising trade and investment, led by a strong power, the US, that has created prosperity the like of which had never been seen before.

Free markets are in the dock today, as the full extent and pain of this crisis is revealed. But as we look beyond the turmoil, and as policymakers consider how to prevent future crises, we must strive at all costs to avoid repeating the protectionist errors of the 1930s. Instead, we must remind ourselves constantly of the immense wealth and prosperity that free markets have helped create for humankind.

This crisis is severe; it is without doubt the most serious for many generations, and it is hard to look beyond the sea of red on trading screens to the future.

Nevertheless, the crisis will pass; trust and confidence must and will be rebuilt. More importantly though, it is important to understand this crisis for what it is and what it isn't. It is not just about a housing bubble in the US, nor just about a consumer debt explosion in the developed world. It is part of a much more fundamental shift in the world economy, from one dominated by a single nation, to one in which wealth is created and shared much more widely -- a world which is more complex and in which international cooperation to ensure stable, efficient, open capital markets becomes more and more important for us all.

Stephen Green is the group chairman of HSBC Holdings. The article (last part) is adapted from his October 20 speech at the FT/DIFC World Financial Centres Summit.