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Eric Pfanner

Publicis chief praises new U.S. message

PARIS

The morning after Barack Obama was elected the next president of the United States last month, Maurice Lévy, chief executive of Publicis Groupe, the advertising company based in Paris, sent an e-mail message to the 15,000 Publicis employees in the United States.

"Congratulations on such a great choice," he wrote. "Once again the American people have proved that they are right there when it comes to turning points in history — and they know how to make history."

In his support for Obama, Lévy had plenty of company in Europe, of course. And Lévy understands the value of friendly relationships with politicians; associates say he uses the informal French "tu," rather than the formal "vous," to address President Nicolas Sarkozy of France.

But openly gushing about the results of another country's election is

U.K. bank rescue plan, a global model, runs into trouble

By Julia Werdigier

LONDON: Gordon Brown's British bank rescue plan was widely praised and quickly emerged as a model for other countries, including the United States, to emulate. But the accolades may have been premature.

Despite the government's aggressive efforts, the plan is in trouble because the banks are resisting pressure to lend more as they seek to protect themselves in the harsh economic climate.

When Brown, the British prime minister, in October, presented the plan to inject capital into banks in exchange for a substantial shareholding, he promised not just to stabilize the British banking system, which threatened to crumble under its exposure to American subprime mortgages and the country's own bursting housing bubble, but also to jump-start the stalled lending market.

The first part worked: The troubled banks were saved and even Barclays, which declined the rescue package, found outside investors to help repair its balance sheet. Brown's popularity ratings surged and some newspapers christened him Flash Gordon.

But less than two months later, the plan is attracting mounting criticism from lenders, economists and opposition politicians for failing to revive lending. Brown on Friday acknowledged the need for more action and said the government was working on a "second stage" of the banking rescue.

Michael Taylor, a senior economist at Lombard Street Research in London, said, "There is no sign yet of significant easing of credit conditions." Taylor added, "In fact some banks are tightening the credit conditions so in that sense the plan's not working."

Britain agreed in October to inject £50 billion, or about $75 billion at current rates, in exchange for large equity stakes it would use to put pressure on the banks to ease lending to businesses and consumers. The biggest beneficiary was Royal Bank of Scotland, and the government plans to sell all of its bank investments back to shareholders once the market recovers. A separate credit line to back interbank lending, along with interest rate cuts and a fiscal stimulus package worth £20 billion, was supposed to further grease the lending market.

Even though interbank lending rates have started to decline slowly since October they remain relatively high as banks continue to hoard capital amid concern about rising loan defaults. Banks failed to fully pass on the recent Bank of England rate cuts to customers; the average cost of a two-year fixed-rate mortgage fell by 0.71 of a percentage point in November compared with a 1.5 point cut in the central bank rate during the same month.

'The economy is threatened to be throttled.'

Some analysts said the idea that a bank recapitalization would repair the lending market was flawed from the beginning. On one hand, the plan aims to pressure banks to reduce risks and return to profitability to quickly repay the government; on the other it is supposed to pressure them to lend more and take on more risk.

"Current policy objectives are conflicting and incoherent," said Michael Coogan, director general of the Council of Mortgage Lenders. "The government needs to decide on its key priority. The tug of war with lenders being pulled in every direction at once needs to end."

Vincent Cable, the finance spokesman for the Liberal Democrats, said the multiple objectives of the recapitalization plan were "canceling themselves out." He said the top priority should be to restore lending or else "the economy is threatened to be throttled."

Brown hoped that the capital injection would give banks enough additional cash to remain liquid while they wrote down toxic assets and rebuilt their balance sheets so that they could lend again. But most banks, hunkering down to survive what is expected to be a long and damaging recession, remain paralyzed.

Alistair Darling, chancellor of the Exchequer, as recently as Wednesday attacked them for not fulfilling their part of the deal, saying that with billions of taxpayers' money invested, the general public was "looking for something in return."

The initial rescue plan had two inherent flaws, some analysts said.

For one thing, the capital injection came in tandem with a requirement that the banks set aside more capital as a cushion against further losses. The cash investment from the government made banks stronger as they faced a worsening economic climate, but it did not give them enough to revive lending, said John Hitchins, head of the British banking team at PricewaterhouseCoopers in London.

The second flaw was that it failed to properly assess the risks associated with toxic assets that remained on the banks' balance sheets. HBOS, the mortgage lender, said Friday that bad loans backed by assets including homes rose 75 percent in the past two months, indicating things might get worse before they got better. At a time when unemployment, home repossessions and loan defaults increase, banks are naturally reluctant to lend.

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period," Haarde said one protester, Stefan Jonsson.

U.S. needs the 'multiplier effect'

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breaks, in contrast, would require the entire $1 trillion in rebates or lower taxes.

"The multiplier effect is clearly less than $1," said Nigel Gault, chief domestic economist for Global Insight, "and perhaps as low as 30 cents if only some of the tax break is spent.'

The one stimulus actually enacted by Congress — a $168 billion package that President George W. Bush signed early this year — consisted entirely of tax breaks, mainly in the form of rebate checks mailed to millions of Americans.

Some of that windfall was saved or it was spent on imports rather than on goods and services produced in the United States. The latter adds to the nation's economic output; the former does not, helping to explain why this first stimulus failed to arrest the economic contraction.

The problem with a stimulus package weighted heavily toward public spending is that there is a shortage of projects on which spending could begin in two or three months. The Economic Policy Institute, for example, has listed $360 billion in ready-to-go work, one-third of it highway and school repair. Zandi offers a similar estimate.

"Still," Zandi said, "if you don't pick a big enough number for a stimulus package now and you have to announce another number next year, people will say, 'Oh, the stimulus didn't work. What makes you think this one will?' "

The financial-sector bailout does not address declining growth.

Until now, big numbers have been noticeably absent from the stimulus debate. The House of Representatives approved a $60 billion package in late September, sending it to the Senate, which has not voted on the measure. The House action was followed in mid-October by talk among the Democratic congressional leadership of upgrading the $60 billion to as much as $200 billion in a lame duck session.

And then a week ago, Senator Charles Schumer, the senior Democrat from New York, suggested that any package should be $500 billion to $700 billion.

"By our estimates," Jan Hatzius, chief domestic economist for Goldman Sachs, said in a newsletter this week, "the private sector retrenchment could subtract an annualized 4 percentage points or about $600 billion from economic growth through the end of 2009."

The financial-sector bailout does not address this decline. Rescuing banks and other lenders has little direct impact on economic growth or job creation. The chief goal of the bailout is to get credit flowing again from reluctant and damaged lenders.

The stimulus package, in contrast, puts up government money as a substitute for the spending and investment that is no longer taking place in the private sector — despite unusually low interest rates — so that the economy can grow again, or at least stop shrinking.

That makes the stimulus package ever more important if the economy continues to deteriorate at its present pace. Not

Chip East/Reuters

Mark Zandi said deciding how much to spend immediately could be critical.

since the first quarter of 1982, in the midst of a severe recession, has the gross domestic product contracted at a 4 percent annual rate in a single three-month period, as a growing number of forecasters say it is now doing, according to Blue Chip Economic Indicators.

In America's giant $14.4 trillion economy, that means the output of goods and services has been declining by nearly $50 billion a month since September. Seldom since the Great Depression has something like that happened.