Financial Times FT.com
Search FT.com
Skip to main content, accesskey 's'
Homepage, accesskey '1'

Sunday Dec 16 2007
All times are London time
Search
Quotes

COMPANIES Financial services
> Financial services

Services
- Email briefings
- Email alerts
- Portfolio
- Currency converter
- Jobs

Subscribe to FT.com or view and edit your subscription details.

Highlight
Special features
Understanding reporting »
Understanding collaboration »

Home
World
- By sector
  - Aerospace & defence
  - Autos
  - Basic industries
  - Consumer industries
  - Drugs & healthcare
  - Energy Utilities
  - Mining
  - IT
  - Media & internet
  - Property
  - Retailing & leisure
  - Telecoms
  - Transport
- By region
- Columnists
- Companies A-Z
- Week in review

Markets
Markets data

- Business for sale
- Contracts & tenders

Helicopters start dropping bundles of cash

By Martin Wolf

Published: December 13 2007 02:00 | Last updated: December 13 2007 02:00

The central bank helicopters are planning a co-ordinated drop of liquidity on troubled market waters. The money to be dropped now is not that large. But if this does not work, more will surely follow. The helicopters will fly again and again and again.

Copyright The Financial Times Limited 2007

Print article Email article Order reprints

More from this sector

Investors pull $1bn from Raptor fund
Weill urges Pandit not to break up Citi
Goldman hired to aid N Rock rescue
Buy-to-let financing in UK evaporates
Close Brothers in takeover talks
UniCredit halves its stake in Mediobanca
HSBC bolsters presence in Taiwan
Tokio Marine snaps up Kiln for £442m
MBF board endorses Bupa's A$2.4bn bid
FSA bans former Insure & Go chief

Latest Companies news

- Weill urges Pandit not to break up Citi
- Goldman hired to aid N Rock rescue

Jobs

Search

Group Accountant
Recruiter: Capital Consulting

Solution Architect
Recruiter: Centrix

Information Risk Managment - Data Modeller
Recruiter: Marks Sattin

Financial & Management Accountant
Recruiter: Robert Half International

Recruiters
FT.com can deliver talented individuals across all industries aro the world
Post a job now

Managed funds
Lex
Comment & Analysis
Technology
Video & Audio
Business Life
Business education
Your Money
Arts & Weekend
Wealth
In depth
Special Reports
Jobs & classified
Services & tools

Blogs

- Brussels Blog
- Charles Pretzlik
- Clive Crook
- Dear Lucy
- Economists' Forum
- Energy Filter
- John Gapper
- Gideon Rachman
- Tech Blog
- The Undercover Economist
- Westminster Blog
- Willem Buiter's Maverecon

Regional pages

- Latin American agenda
- China
- India
- Brussels

Interactive

- Podcasts
- Debates & polls
- Ask the expert
- Markets Q&A

One point is clear: central banks must be pretty worried to take such a joint action. For what is remarkable about yesterday's statement is that five central banks - the Bank of Canada, the Bank of England, the European Central Bank, the Federal Reserve and the Swiss National Bank - are co-ordinating their (different) interventions. Their hope must be that this action will trigger not panic ("What do the central banks know that I do not?") but confidence ("Now that the central banks are prepared to intervene in this way, I can at last stop worrying").

It is easy to

- **Strike threat adds to Alitalia's woes**
- **Google in challenge to Wikipedia**
- **Siemens retracts key promotion**
- **Buy-to-let financing in UK evaporates**
- **US sales of PlayStation 3 leap by 300%**
- **Lufthansa sure deal won't take shine off Star**

Related Services

- UK annual reports
- Market research
- Growth companies
- Free Technology white papers and trials
- FT Fine Wine Plan
- FT Diaries
- FT Bookshop
- FT Conferences
- FT Syndication services

understand why central banks should have decided to take heroic action. Confidence has fled the markets in a four-month long episode of "revulsion". As a result, monetary policy is not being transmitted to the ultimate borrowers as central banks wish. Particularly worrying has been the widening of gaps between three-month interbank lending rates and policy rates in the dollar, euro and sterling markets. Spreads in the last of these have recently become enormous (at more than 100 basis points).

Yet this is not the only indication of distress: in the US, for example,

the spread between the rate of interest on three-month treasury bills and AA-rated asset-backed financial paper has widened to 270 basis points from 30 basis points earlier in the year. This is revulsion, indeed.

So why might yesterday's co-ordinated interventions succeed where previous actions have not?

In a word, the answer is: stigma.

Central banks have become increasingly worried about the unwillingness of banks to borrow from them. These banks reasonably fear that exceptional borrowing is a signal mainly of distress. The hope of the central bankers is

that by auctioning funds to a wide group of institutions such anxiety would diminish, if not disappear. That hope is strengthened by the fact that these actions are joint: they are evidently aimed at lifting sentiment rather than saving specific institutions.

Will this work? The answer is that if the fundamental problem in the markets is lack of liquidity (that is, panic), rather than insolvency, and if central banks are believed willing to offer liquidity to solvent institutions without limit at what the latter consider a "reasonable" discount, then symptoms of stress

should indeed disappear.

Yet these are both important provisos. In particular, there is good reason to believe that a good part of the stress is caused by worries over solvency, indeed by the reality of threatened insolvency in at least some cases. True, central banks or, more precisely, the treasuries that stand behind them, could eliminate that concern, too, by buying up every piece of paper, good, bad and indifferent. But that would also be an open-ended, possibly very expensive and certainly unpopular bail-out.

Moreover, even if

today's stress is indeed a liquidity problem (something that we do not now know), there remains the question of the scale of the intervention required. Assume, for example, that central banks end up buying a vast amount of paper and so providing liquidity to institutions that have deliberately taken on big risks, by lending long and borrowing short. They have then validated those strategies, after the event.

So does the action by the central banks give us good reason to stop worrying? Only if you like huge rescue operations of incompetent bankers,

would be my answer. They may well get the markets back into order. They may, in this way, rescue economies from the threat of recessions. But that is not the end of the story. The bigger the rescue today, the more stringent regulation of financial institutions must be in future.

Recent reports

Market research reports

Report name	Author	Publish date	Cost
Teens, Money, Payment Cards and...........	Packaged Facts	1/1/2008	$3850
Insurance Carriers	First Research, Inc.	12/10/2007	$129
Title Insurance Services	First Research, Inc.	12/10/2007	$129
Real Estate Investment Trusts (REITs)	First Research, Inc.	12/10/2007	$129
Insurance Agencies	First Research, Inc.	12/10/2007	$129

- **Free annual reports**

* Minimum delay 15 minutes All times are London time

FT Home

Advertise with the FT Media centre Student offers FT Conferences FT Syndication Corporate subscriptions FT Group

Partner sites: Chinese FT.com Les Echos FT Deutschland Expansion Investors Chronicle Exec-Appointments.com

© Copyright The Financial Times Ltd 2007. "FT" and "Financial Times" are trademarks of The Financial Times Ltd. Privacy policy Terms