Europe's financial lifeline from London in doubt

FRANKFURT: For companies in the European Union, London is the chief gateway to finance. Rerouting the financial lines that run through London will be complex, experts say.

London dominates wholesale banking in Europe, a 5.8 trillion euro ($6.2 trillion) industry that includes financing for companies from big multinationals to family-owned firms that are the backbone of Germany's economy. London is also the first port of call for companies, such as Italian lender UniCredit, selling shares or raising debt. This is because many fund managers and asset managers have a base in Britain. The Bank of England estimates that half of the debt and equity issued by EU borrowers involves financial groups in Britain. This could be a London bank organising a sale of European company bonds, for example.

And London houses the bulk of Europe's derivatives market, where car makers buy protection against swings in the US dollar or airlines guard themselves against a spike in the price of oil. More than 7 trillion euros of trading in such instruments is processed in London daily.

Experts expect EU firms and banks gradually to reduce their reliance on London. Governments in France and Germany want to establish alternatives to London in Paris and Frankfurt.

Over time, some of London's wholesale funding will move to other centres in Europe. Thinktank Bruegel predicts that London's share of this market will eventually shrink from 90 percent to 60 percent. If mismanaged, however, the migration could raise the cost of funding for European companies, the thinktank said.

Bruegel's Dirk Schoenmaker said that if wholesale funding operations are spread across several locations that could lift costs by between 6 billion and 12 billion euros each year because of the expense of using multiple financial centres. That is equivalent to up to 0.1 percent of the remaining 27 EU countries' economic output. Shifting the multi-trillion euro derivatives business would be difficult, regulators and bankers said. Some derivatives have a term of many decades. It is unclear, bankers said, what will happen when Britain, where the contracts were drafted, leaves the European Union.

They said that the cost of holding such instruments could rise sharply for European banks if a clearing house in London that processes the deal, for example, is not recognised in the European Union. A transition period, after initial exit talks of two years, could win extra time. But many bank executives, speaking privately, have said they are working on the assumption that there will be no transition.

EU officials familiar with the bloc's preparations for negotiations have told Reuters that they too fear a "cliff-edge" departure of Britain from the bloc. They are pinning their hopes on banks moving to the continent in time and believe this will minimize any fallout for their economies. — Reuters

PARIS: French Junior Minister for Budget Christian Eckert (right) listens to Finance minister Michel Sapin speaking during a press conference to present the latest figures on France's public deficit yesterday at the Economy ministry in Paris. — AFP

Eurozone economy sparkles, lights way for ECB pull-back

France, Germany heading for Q1 growth

LONDON: If the latest surveys of business intentions are to be believed, the euro-zone economy is sparkling, growing at a pace that easily explains the hints from some European Central Bank policymakers of a pull-back from their easy-money regime. IHS Markit's euro zone Flash Composite Purchasing Managers' Index (PMI), an influential guide to the buying plans of businesses and hence growth, hit a near six-year high this month.

It climbed to 56.7 from February's 56.0, its highest reading since April 2011 and better than any predictions in a Reuters poll. At the same time, flash surveys for the currency bloc's two largest economies-Germany and France-also stormed past expectations to register near six-year highs, conditions likely to play into elections in both countries this year.

"This is a really solid rate of expansion. It's an economy firing on all cylinders," Chris Williamson, chief business economist at IHS Markit, said of the euro zone.

He added that it implied first quarter economic growth of 0.6 percent quarter on quarter, which would be the joint highest reading since the first quarter of 2011.

One immediate impact may be to put pressure on the ECB to begin rolling back its historically easy monetary policy, a combination of zero to negative interest rates and a large asset-buying program.

Earlier this month the ECB pledged to extend its bond-buying program to at least the end of the year, citing weak underlying inflation and lacklustre growth in the euro zone. It will, however, reduce its monthly spend from April. It also highlighted that it no longer felt a "sense of urgency" to take further action. Since then some ECB policymakers, notably Austria's Ewald Nowotny and Italy's Ignazio Visco, have spoken of a rate hike within or just after the period of the bond-buying program.

"These (PMI) numbers will likely reinforce the ECB's view that downside risks are diminishing. But the central bank will only tighten gradually," Morgan Stanley said in a note. The key will be inflation, control of which is the ECB's primary mandate. Markit's euro zone PMI sub-index measuring prices charged by businesses rose to a near six-year high of 53.3.

Inflation in the euro zone was 2.0 percent in February- around the ECB's target.

"What we are picking up is an increase in suppliers' ability to hike prices due to strong demand. If that continues to intensify the ECB should become more worried," Markit's Williamson said.

Fracturing the forecasts

All nine of yesterday's PMI reports-manufacturing, services and composite for the eurozone, France and Germany-beat even the most optimistic forecasts in Reuters polls of economists. France's composite registered 57.6 in March from 55.9 in February, a particularly significant rise given the country's economy is generally lagging and this put it above Germany. How such data plays into the French presidential election, the first round of which is in April, remains to be seen.

National Front candidate Marine Le Pen will be hoping to capture votes from those angry with their economic lot. But the two other leading candidates, Emmanuel Macron and Francois Fillon are both calling for economic reform. A hefty chunk of the electorate has yet to decide who to vote for, if the polls are anything to go by. — Reuters

Sri Lanka raises rates as growth slows, inflation spikes

COLOMBO: Sri Lanka raised its key interest rate by 25 basis points yesterday as inflation spiked and foreign reserves fell, compounding problems caused by slowing economic growth.

The Central Bank of Sri Lanka said it raised the benchmark lending rate from 8.5 percent to 8.75 percent as year-on-year inflation increased to 8.2 percent last month, sharply up from 6.5 percent in January. Sri Lanka enjoyed blistering economic growth rates averaging more than 8.0 percent for two years after a prolonged civil war ended in 2009.

But growth has been slowing ever since, hitting 4.4 percent last year, according to central bank data. Foreign reserves fell to $5.6 billion at the end of February compared to $6.0 billion in December 2016. "The Monetary Board was of the view that further tightening of monetary policy is necessary as a precautionary measure, in order to contain the buildup of adverse inflation expectations," it said.

A drought gripping parts of the island and unfavourable external conditions were hurting the economy, the bank said. Last June, the government received a $1.5 billion bailout from the IMF after facing a balance of payments crisis.

Earlier this month, the IMF said Sri Lanka's current account remained stable, but the financial account weakened with the resumption of capital outflows. The IMF also warned that a prolonged drought in the island could raise food and oil imports with adverse impacts on economic growth, inflation, and the country's balance of payments. — AFP

UK consumers spend more in February

LONDON: Official figures show retail sales in Britain bounced back strongly in February but that the underlying picture remains gloomy as the country prepares to start two years of discussions to leave the European Union. The Office for National Statistics said Thursday that retail sales rose 1.4 percent in February from the previous month. An increase had been expected following three monthly declines. On a three-month basis, however, retail sales are still down by 1.4 percent. That's the worst three-month performance since March 2010.

Analysts say the underlying picture suggests that households are reining in spending ahead of Prime Minister Theresa May's upcoming triggering of the two-year Brexit process as well as rising inflation largely related to higher energy prices. — AP